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In The

Supreme Court of the United States

October Term, 1996

AMERICAN PUBLIC GAS ASSOCIATION and
CITIZENS GAS & COKE UTILITY,

Petitioners,

vs.

FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the United States Court of Appeals for the District of Columbia Circuit erred in holding that the Federal Energy Regulatory Commission acted within its jurisdictional mandate in extending the provisions of its natural gas capacity release program (promulgated under the Natural Gas Act, 15 U.S.C. § 717 *et seq.*) to municipalities which are exempt from FERC regulation under the plain meaning of the Natural Gas Act.

PARTIES TO THE PROCEEDING

Pursuant to Rules 14.1(b) and 29.6 of the Rules of the Supreme Court of the United States, Petitioners state as follows:

American Public Gas Association

The American Public Gas Association ("APGA") is a national not-for-profit association of over 460 municipal and other publicly-owned local distribution systems in thirty six states that provide natural gas distribution service to the communities in which they are located. APGA was founded in 1961 for the purposes, among others, of enhancing the safety, reliability, service and competitiveness of publicly-owned gas distribution systems and to participate in state and federal policymaking decisions that affect the operations of public gas systems.

All of APGA's full members are political subdivisions of states, *e.g.*, municipalities, utility boards, and utility districts. APGA also allows businesses serving the natural gas distribution industry to join as "associate members."

Citizens Gas & Coke Utility

Citizens Gas & Coke Utility ("Citizens"), the City of Indianapolis' municipal gas distributor, provides natural gas for public consumption to approximately 250,000 customers in Indianapolis and Marion County, Indiana.

In addition to the above Petitioners, the following were parties to the proceeding before the court of appeals:

Federal Energy Regulatory Commission (Respondent)

Alabama Gas Corporation (Intervenor)

Algonquin Gas Transmission Company (Intervenor)

Allied Signal Inc. (Intervenor)

American Forest & Paper Association (Petitioner)

American Public Gas Association (Petitioner)

Amoco Production Company (Intervenor)

Anadarko Petroleum Corporation (Intervenor)

ANR Pipeline Company (Intervenor)

Arcadian Fertilizer (Petitioner)

Arco Natural Gas Marketing (Intervenor)

Arco Oil & Gas Company (Intervenor)

Arizona Electric Power Cooperative Inc. (Petitioner)

Arizona Public Service Company, *et al.* (Petitioner)

Asarco, Inc., Cyprus Miami Mining Corporation, and Magma Copper Company (Petitioner)

Associated Gas Distributors (Petitioner)

Associated Natural Gas Company (Petitioner)

Atlanta Gas Light Company (Petitioner)

Baltimore Gas & Electric Company (Petitioner)

Bay State Gas Company, *et al.* (Intervenor)

Board of Water, Gas & Light Commissioners, Albany, Georgia (Intervenor)

Brooklyn Union Gas Company (Intervenor)

Canadian Association of Petroleum Producers, *et al.* (Intervenor)

Carnegie Natural Gas Company (Petitioner)

Chattanooga Gas Company (Petitioner)

Cascade Natural Gas Corporation (Intervenor)

Chevron, U.S.A., Inc. (Intervenor)

Cincinnati Gas & Electric Company, *et al.* (Intervenor)

Citizens Gas & Coke Utility (Petitioner)

City of Hamilton, Ohio (Petitioner)

CNG Transmission Corporation (Petitioner)

Colorado Interstate Gas Company (Petitioner)

Colorado Springs Utilities (Petitioner)

Columbia Gas Distribution Companies (Intervenor)

Columbia Gas Transmission Corporation (Intervenor)

Conoco, Inc. (Intervenor)

Consolidated Edison Company of New York, Inc. (Petitioner)

Dakota Gasification Company (Intervenor)

Dayton Power & Light Company (Intervenor)

Destec Energy, Inc. (Intervenor)

East Ohio Gas Company, *et al.* (Intervenor)

East Tennessee Group (Petitioner)

East Tennessee Natural Gas Company (Intervenor)

Elizabethtown Gas Company, an Operating Division of NUI Corporation (Petitioner)

El Paso Natural Gas Company (Intervenor)

Enron Oil & Gas Marketing, Inc. (Intervenor)

Enserch Development Corporation (Petitioner)

Equitrans, Inc. (Petitioner)

Exxon Corporation (Intervenor)

Florida Cities (Intervenor)

Florida Gas Transmission Co. (Intervenor)

Foothills Pipelines Ltd. (Intervenor)

Fort Pierce Utilities Authority and the City of Vero Beach, Florida (Intervenor)

Fuel Managers Association (Intervenor)

Georgia Industrial Group (Petitioner)

Great Lakes Gas Transmission Ltd. (Intervenor)

Hadson Gas Systems, Inc. (Petitioner)

Illinois Commerce Commission (Petitioner)

Illinois Power Company (Petitioner)

Indiana Gas Company (Petitioner)

Interstate Natural Gas Association of America (Intervenor)

Joint State Commissions and Consumer Advocates (Petitioner)

KN Energy, Inc. (Intervenor)

Kern River Gas Transmission Company (Petitioner)

Koch Gateway Pipeline Company (Petitioner)

Laclede Gas Company (Petitioner)

Long Island Lighting Company (Petitioner)

Louisville Gas & Electric Company (Petitioner)

Maryland Office of People's Counsel (Petitioner)

Maxus Exploration Company and Maxus Gas Marketing Company (Intervenor)

Memphis Light, Gas and Water Division (Petitioner)

Meridian Oil Inc. (Petitioner)

Michigan Consolidated Gas Company (Intervenor)

Midland Cogeneration Venture Limited (Petitioner)

Minnesota Public Utility Commission and Minnesota Department of Public Service (Intervenor)

Mississippi River Transmission Corporation (Intervenor)

Missouri and Kansas Gas Users (Intervenor)

Missouri Public Service Commission, *et al.* (Petitioner)

Mitchell Energy Corporation (Intervenor)

Mobile Gas Service Corporation, *et al.* (Intervenor)

Mobil Natural Gas, Inc. (Intervenor)

Montana Public Service Commission, Public Utilities Commission of South Dakota and Montana Consumer Counsel (Petitioner)

Mountaineer Gas Company (Petitioner)

National Association of State Utility Consumer Advocates (Petitioner)

National Association of Gas Consumers (Intervenor)

National Fuel Gas Supply Corporation (Intervenor)

Natural Gas Clearinghouse (Intervenor)

Natural Gas Pipeline Company of America (Intervenor)

New Jersey Board of Regulatory Commissioners (Petitioner)

New Jersey Natural Gas Company (Petitioner)

New York State Electric & Gas Corporation (Intervenor)

New England Power Company (Petitioner)

Northern Indiana Public Service Company (Petitioner)

Niagara Mohawk Power Corporation (Petitioner)

NorAm Energy Corporation (Petitioner)

North Carolina Natural Gas Company and Public Service Commission of North Carolina (Intervenor)

Northeast Energy Associates and New Jersey Energy Associates (Intervenor)

Northern Border Pipeline Company (Intervenor)

Northern Distributor Group (Intervenor)

Northern States Power Company (Minn.), *et al.* (Intervenor)

Northern Natural Gas Company, *et al* (Intervenor)

Northwest Alaskan Pipeline Company (Petitioner)

Ocean State Power, *et al.* (Petitioner)

Office of the Consumers' Counsel, State of Ohio (Petitioner)

Orange and Rockland Utilities, Inc. (Petitioner)

Ozark Gas Transmission System (Petitioner)

Pacific Gas & Electric Company (Petitioner)

Pacific Interstate Transmission Company, *et al.* (Intervenor)

Pan-Alberta Gas, Ltd. (Intervenor)

Panhandle Customer Group (Intervenor)

Panhandle Eastern Pipe Line Company (Intervenor)

Panhandle Trading Company (Intervenor)

Pennzoil Exploration & Production Company and Pennzoil Gas Marketing Company (Intervenor)

PEPCO Energy (Petitioner)

Pennsylvania Office of Consumer Advocate (Petitioner)

Pennsylvania Public Utility Commission, *et al.* (Petitioner)

Peoples Gas System, Inc. (Intervenor)

Peoples Natural Gas Company (Petitioner)

Piedmont Natural Gas Company (Petitioner)

Philadelphia Electric Company (Petitioner)

Phillips Petroleum Company, *et al.* (Intervenor)

Plains Petroleum Operating Company (Petitioner)

Process Gas Consumers Group, *et al.* (Intervenor)

Producer-Marketing Transportation Group (Petitioner)

ProGas, Ltd. (Petitioner)

Public Service Commission of the Commonwealth of Kentucky (Petitioner)

Public Service Commission of Nevada (Intervenor)

Public Service Commission of the State of New York (Petitioner)

Public Service Commission of West Virginia, Consumer Advocate Division (Petitioner)

Public Service Commission of Wisconsin (Petitioner)

Public Service Electric & Gas Company (Intervenor)

Public Utilities Commission of the State of California (Petitioner)

Rochester Gas & Electric Company (Intervenor)

Shell Gas Trading Company (Intervenor)

South Jersey Gas Company (Intervenor)

South Carolina Pipeline Corporation (Intervenor)

Southern Natural Gas Company (Intervenor)

Southwest Gas Corporation (Petitioner)

State of Louisiana (Petitioner)

State of Indiana, Office of Utility Consumer Counselor (Petitioner)

Tenneco Gas, Inc. (Intervenor)

Tennessee Gas Pipeline Company (Intervenor)

Tennessee Small General Service and Columbia Small Customer Group (Intervenor)

Tennessee Valley Municipal Gas Association (Petitioner)

Texaco, Inc. (Intervenor)

Texas Eastern Transmission Corporation, *et al.* (Intervenor)

TransCanada Pipelines Limited (Intervenor)

Transcontinental Gas Pipe Line Corporation (Intervenor)

Transwestern Pipeline Company (Intervenor)

Trunkline Gas Company (Intervenor)

T.W. Phillips Gas & Oil Company (Intervenor)

UGI Utilities, Inc. (Intervenor)

Union Pacific Fuels, Inc. (Intervenor)

United Cities Gas Company (Intervenor)

United Distribution Companies (Petitioner)

Vastar Resources, Inc. and Vastar Gas Marketing, Inc. (Intervenor)

Virginia Electric & Power Company (Petitioner)

Washington Gas Light Company (Intervenor)

Williams Gas Marketing Company (Petitioner)

Williams Natural Gas Company (Petitioner)

Williston Basin Interstate Pipeline Company (Petitioner)

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The American Public Gas Association and Citizens Gas & Coke Utility [hereinafter collectively referred to as "Petitioners"] respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. at 1a-147a)[1] is reported at *United Distribution Companies v. Federal Energy Regulatory Commission*, 88 F.3d 1105 (D.C. Cir. 1996) ("*UDC v. F.E.R.C.*"). The opinions of the Federal Energy Regulatory Commission ("FERC" or "Commission") reviewed by the court of appeals are reported at *Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation Under Part 284 of the Commission's Regulations, and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, "Order No. 636", F.E.R.C. Stats. & Regs. (CCH) ¶ 30,939 (Pet. App. at 175a-407a), *order on reh'g*, "Order No. 636-A", F.E.R.C. Stats. & Regs. (CCH) ¶ 30,950 (Pet. App. at 408a-812a), *order on reh'g*, "Order No. 636-B", 61 F.E.R.C. ¶ 61,272 (1992) (Pet. App. at 813a-998a), *reh'g denied*, 62 F.E.R.C. ¶ 61,007 (1993) (Pet. App. at 999a-1000a).

STATEMENT OF JURISDICTION

The court of appeals entered its judgment on July 16, 1996. Additionally, the court of appeals denied timely petitions for rehearing and timely suggestions for rehearing *en banc* on October 29, 1996 (Pet. App. at 1005a-06a). The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1) (1994) and 15 U.S.C. § 717r(b) (1994).

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1. An appendix containing the opinion of the court of appeals and its opinions on rehearing, as well as the several lengthy FERC orders that give rise to those opinions, is being filed jointly by the several petitioners for writ of certiorari of the court of appeals' decision.

STATUTORY PROVISIONS INVOLVED

Section 1(b) of the Natural Gas Act, 15 U.S.C. § 717(b) (1994) (Pet. App. at 1007a-08a), provides that:

> [t]he provisions of this chapter shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

Section 1(c) of the Natural Gas Act, 15 U.S.C. § 717(c) (1994) (Pet. App. at 1008a), provides in pertinent part that:

> [t]he provisions of this chapter shall not apply to any person engaged in or legally authorized to engage in the transportation in interstate commerce or the sale in interstate commerce for resale, of natural gas received by such person from another person within or at the boundary of a State if all the natural gas so received is ultimately consumed within such State, or to any facilities used by such person for such transportation or sale, provided that the rates and services of such person and facilities be subject to regulation by a State commission. The matters exempted from the provisions of this

> chapter by this subsection are hereby declared to be matters primarily of local concern and subject to regulation by the several States.

Section 2 of the Natural Gas Act, 15 U.S.C. § 717a (1994) (Pet. App. at 1010a-11a), the definitional section of the Act, defines a "natural gas company" as a "person engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale"; defines a "person" as an "individual" or a "corporation"; and defines a "municipality" as a "city, county, or other political subdivision or agency of a State," but not an individual or corporation.

STATEMENT OF THE CASE

Petitioners, municipalities as defined in Section 2 of the Act ("municipalities"), seek review because the court of appeals' judgment permits FERC to exceed its authority by regulating the activities of Petitioners, which are expressly exempted from FERC's jurisdiction. The predicate of the argument is the statutory framework supplied by the Natural Gas Act ("NGA" or "Act"). 15 U.S.C. § 717 *et seq.* (1994).

A. The Procedural Course of the Agency Proceedings.

1. Order No. 636 and Capacity Release.

Over the last decade, the Commission has taken steps to "restructure" the natural gas industry. During that period, the Commission has allowed market forces to play a more dominant role. The orders on review, Order No. 636, *et seq.*, are the latest in a series of FERC orders intended to restructure the natural gas industry along more competitive lines. FERC claims that these initiatives "finalize" the structural changes it has approved

in recent years and "complete the evolution" to a more competitive market. Pet. App. at 176a-77a.

The principal innovation of Order No. 636 was FERC's directive to the pipelines to "unbundle" their sales and transportation functions. As a result, pipelines exited the gas sales business and became transporters only, and unregulated entities assumed the sales function. Most pertinent here, the Commission promulgated new regulations setting out the procedures under which firm shippers on interstate gas pipelines can temporarily release their transportation capacity to other shippers.[2] *See* Pet. App. at 243a-45a. The Commission did so through the exercise of its jurisdiction to regulate pipelines' terms and conditions of service and rates. Under these "capacity release" procedures, pipeline shippers can resell their firm gas transportation capacity rights.[3] Such resales, which must be made in a non-discriminatory fashion, can be made on a temporary or permanent basis, through either prearranged transactions or by "posting" an offer to release firm capacity on the pipeline's electronic bulletin board.[4] When firm capacity is posted for competitive bidding on the bulletin board, it is awarded to the entity making the best bid according to the criteria established by the firm shipper releasing the capacity.

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2. "Firm shippers" are pipeline customers who have paid for the right to have natural gas transported on their behalf by the interstate pipeline without interruption.

3. Generally speaking, "capacity" is an ownership right held by a shipper on an interstate pipeline that determines the amount of natural gas that the pipeline is obligated by contract to transport for the particular shipper.

4. The electronic bulletin board is nothing more than an informational posting center whereby firm shippers desirous of obtaining or selling capacity on an interstate pipeline can notify other pipeline customers of their intent.

2. Capacity Release Programs and Municipalities.

In Order No. 636-A, the Commission declared that municipalities must comply with the capacity release programs. In doing so, the Commission effectively abrogated its prior decisions holding that the Commission lacks NGA jurisdiction over municipalities. The Commission in Order No. 636-A "agree[d] with [Petitioners] that municipalities are beyond the jurisdiction of the Commission." Pet. App. at 474a-77a. Nonetheless, FERC required municipalities to comply with all of its pipeline capacity release procedures, and justified its regulation of municipalities in this respect solely on the ground that the pipelines' role in the capacity release mechanism is essential.[5] This limited analysis was FERC's sole effort to justify its assertion of jurisdiction over municipalities.

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5. Explaining its holding that municipalities are beyond the jurisdiction of the Commission, FERC stated:

> this means only that municipalities need not be certificated to transport gas on their own systems or to participate in jurisdictional capacity brokering or releasing mechanisms. However, this does not mean that municipalities are entitled to release capacity on an interstate pipeline without complying with the procedures pertinent to the pipeline's releasing mechanism. It means only that the municipalities need not be certificated to release capacity. The Commission's clarification in *Texas Eastern Transmission Corp.* [48 F.E.R.C. ¶ 61,248 (1989), *order on reh'g*, 51 F.E.R.C. ¶ 61,170 (1990)], that "all the conditions imposed upon program participants do not apply to municipalities" is not applicable where the conditions pertain to the mechanics of the release by and through the pipeline. In that circumstance, the capacity releasing mechanism is no different from any other pipeline term or condition of service with which the municipality must comply.

Pet. App. at 476a-77a (footnotes omitted).

Based on FERC's jurisdictional overreaching, Petitioners sought rehearing. In Order No. 636-B, the Commission reaffirmed its position:

> [W]hile municipalities are beyond the jurisdiction of the Commission, they may release capacity on a pipeline only by complying with the procedures pertinent to the pipeline's releasing mechanism because the conditions of the program pertain to the mechanics of the release by and through the pipeline.

Pet. App. at 858a-59a. This ended FERC's review of the capacity release issue as it affects municipalities.

Throughout the Order No. 636 series, the Commission claimed that it was not asserting NGA jurisdiction over municipalities by requiring them to comply with its mandated "mechanical" requirements in releasing their capacity. However, in declaring its authority to determine whether, at what price, and to which shippers municipalities may release their capacity, the Commission has effectively asserted jurisdiction over them. This *de facto* assertion of jurisdiction violates the NGA.

B. Statutory Bases for the Case.

1. Overview.

Congress established a comprehensive regulatory scheme for the natural gas industry in the NGA. Congress granted the Federal Power Commission ("FPC"), the predecessor of FERC, jurisdiction over the sales for resale of natural gas in interstate commerce, as well as the transportation of natural gas in interstate commerce.

There are approximately 1,000 municipalities that own and operate their natural gas distribution systems which, under the NGA, do not come under FERC's jurisdiction. The rates and services of municipalities are regulated by local boards, city councils, or sometimes state agencies. FERC's effective assertion of jurisdiction over municipalities pursuant to Order No. 636, which is contrary to the express language of Section 2 of the NGA, will improperly obstruct their business arrangements with third party end-users within their own service area. It is this aspect of the court's decision with which Petitioners take issue.

2. Municipalities, By Definition, Are Exempt From FERC's Jurisdiction.

Section 1(b) of the Act determines FERC's jurisdiction. Pet. App. at 1007a-08a. Congress empowered the Commission to regulate the transportation of natural gas in interstate commerce, the sale of natural gas in interstate commerce for resale, and natural gas companies engaged in such transportation or sale. *Panhandle Eastern Pipe Line Co. v. Public Serv. Comm'n*, 332 U.S. 507, 516 (1947). Congress' intent was clear. The Act did not reference any other type of natural gas sales and by necessary inference excluded direct sales for consumptive use and the transportation of natural gas on a local level. These are precisely the activities in which municipalities typically engage.

Under Section 2 of the NGA, Pet. App. at 1010a, which has remained unchanged since the Act was introduced in the 74th Congress in 1935,[6] Congress expressly exempted municipalities from the Commission's jurisdiction. The Commission's jurisdiction under the Act, *see* NGA Section 1(b), extends only to "natural gas companies," defined in Section 2(6) of the Act

6. The paragraph and section numbers at times did change with successive versions of the bill.

as "a person engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale." Section 2(1) of the Act defines a person to include "an individual or a corporation." And Section 2(2) defines a "corporation" to include "any corporation, joint-stock company, partnership, association, business trust, organized group of persons, whether incorporated or not, receiver or receivers, trustee or trustees of any of the foregoing, but shall not include municipalities as hereinafter defined." Municipalities are defined in Section 2(3) of the Act as a "city, county, or other political subdivision or agency of a State."

Thus, because a "natural gas company" must be a "person," and a "person" can only be an "individual" or a "corporation," and a municipality is neither an "individual" nor a "corporation," Congress did not give to FERC the power to exercise jurisdiction over municipalities. Indeed, FERC has repeatedly recognized this fundamental fact. *See* discussion *infra.*

In light of FERC's exercise of jurisdiction over municipalities, Citizens and APGA, among others, filed with the United States Court of Appeals for the District of Columbia Circuit timely petitions for review of Order No. 636. Upon review, the court affirmed FERC's holding in Order No. 636 that FERC could regulate the capacity release transactions of municipalities.

REASONS FOR GRANTING THE WRIT

I.

THE COURT OF APPEALS' DECISION IGNORES THE PLAIN MEANING OF THE STATUTE AND CONFLICTS WITH DECADES OF COURT AND FERC PRECEDENT.

A. The NGA's Plain Meaning Must Be Enforced.

This is a case in which the court of appeals has ignored the plain meaning of the governing statute. Any interpretation of the NGA and the Commission's power to regulate the capacity release of municipalities must rest on a firm understanding of congressional purpose in enacting the NGA. *See, e.g., Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 533 (1992) (Blackmun, J., concurring in judgment in part). This Court need not go beyond the language of the NGA to determine whether Congress intended the Commission to have jurisdiction over municipalities. *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984) ("If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress."); *see also Medtronic Inc. v. Lohr*, __ U.S. __, 116 S. Ct. 2240, 2250-51 (1996) (citation omitted). Congress' intent is clearly stated in Section 2 of the NGA. 15 U.S.C. § 717a.

Moreover, the legislative history of the NGA reveals Congress' express intention that the Act leave regulation of local distribution service exclusively at the local level. H.R. Rep. No. 709, 75th Cong., 1st Sess. (1937). ("[T]he whole purpose of this Bill is to bring under Federal regulation the pipelines and to leave to the State commissions control over distributing

companies and over their rates, *whether that gas moves in interstate commerce or not.*") (emphasis supplied).

The specific language of the NGA both grants regulatory jurisdiction to the Commission in certain instances with respect to the transportation of natural gas and provides limitations on that jurisdiction with respect to municipalities. The court of appeals' finding that the Commission has jurisdiction over a municipality's capacity release transactions "given the involvement of interstate gas pipelines" (Pet. App. at 84a) is unsupported by the text of the NGA or the legislative framework surrounding it. *See generally* H.R. Rep. No. 709, 75th Cong., 1st Sess. (1937). It is clear that Congress anticipated the "involvement of interstate gas pipelines" with the activities of municipalities. *Id.* Thus, if Congress had intended that municipalities be subject to the Commission's jurisdiction when their activities "involved interstate gas pipelines," it would have so stated.

Instead, Congress struck the balance between the appropriate realm of federal regulation and the appropriate realm of local regulation and reflected it in the express terms of the NGA. *See* 15 U.S.C. §§ 717(b) and 717a. FERC's attempt to gain jurisdiction over municipalities indirectly through its exercise of jurisdiction over a pipeline's transportation capacity has the effect of usurping the authority of non-jurisdictional municipalities.

The court of appeals, by its opinion, upset Congress' intended jurisdictional balance by improperly endorsing the Commission's regulation beyond the mandated federal sphere into "matters primarily of local concern." 15 U.S.C. § 717(c). Permitting such overreaching by a federal agency is prohibited under the principles of federalism. *See Gregory v. Ashcroft*, 501 U.S. 452, 460 (1991).

The Supreme Court should intervene in cases such as this, where the federal government's regulation upsets the federal-municipal balance to such a degree that it usurps the traditional authority of local governments and thus violates the principles of federalism. *Id.*; *see also United States v. Lopez*, __ U.S. __, 115 S. Ct. 1624, 1639-40 (1995) (Kennedy, J., concurring).

FERC itself does not quarrel with the fact that municipalities are exempt entities under Section 2 of the NGA: "FERC wholly 'agrees with [petitioners] that municipalities are beyond [its] jurisdiction.' " Pet. App. at 84a. Despite the Commission's concession, the court of appeals erroneously applied its own tortured statutory construction of the NGA in order to justify the Commission's jurisdiction. The court of appeals improperly read the broad language in Section 1(b) of the NGA stating that the Commission has jurisdiction over the "interstate transportation of natural gas" as bringing the municipality's capacity release transactions under the Commission's jurisdiction. Pet. App. at 83a. In so doing, the court of appeals effectively held that the *broad* jurisdictional statement in Section 1(b) overrides the very *specific* exclusion of municipalities from the Commission's jurisdiction in Section 2 of the NGA. *See* Pet. App. at 83a-84a. The court of appeals provided no meaningful explanation or analysis of this untenable construction of the NGA.

Under the holding in *UDC v. F.E.R.C.*, the Commission, through its jurisdiction over the terms and conditions of interstate pipelines' transportation services and the rates charged for these services, will now be able to dictate when municipalities can release their capacity to third party customers, which third party customers they can release to, and the appropriate price a municipality can charge for its products and services. The court of appeals' decision effectively expands FERC's statutory responsibilities and, in so doing, affords the Commission, in

direct conflict with the NGA, the ability to regulate municipalities.[7]

B. Conflict with Past Precedent.

In almost sixty years of NGA jurisprudence, the courts and FERC have carefully observed the statutorily-imposed constraint upon the scope of the Commission's interstate commerce jurisdiction. Notwithstanding the courts' *and* FERC's consistent refusal to expand FERC's jurisdiction over municipalities in the absence of an express act of Congress granting such authority, that is the result of Order No. 636 and of the court's holding in *UDC v. F.E.R.C. See generally F.P.C. v. Louisiana Power & Light Co.*, 406 U.S. 621, 635-36 (1972) ("[A] need for [comprehensive] federal regulation does not establish FPC jurisdiction that Congress has not granted.").

The crux of the court of appeals' reasoning in *UDC v. F.E.R.C.* is its agreement with FERC that the agency's jurisdiction over the transportation of natural gas in interstate commerce extends to capacity release. The court held:

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7. This is especially important because FERC paradoxically is expanding its jurisdiction at the same time it is pursuing deregulation. Emboldened by the court of appeals' decision, FERC subsequently has attempted to assert jurisdiction over the transportation programs of local distribution companies ("LDCs") (which are also exempt from FERC jurisdiction) behind their city-gates, claiming that their activities are but an extension of the interstate market. *See Secondary Market Transactions on Interstate Natural Gas Pipelines, Proposed Experimental Pilot Program to Relax the Price Cap for Secondary Market Transactions*, 61 Fed. Reg. 41,401 (Aug. 8, 1996) ("LDCs need to meet the NOPR's requirements for open access service") (citing Secondary Market Transactions on Interstate Natural Gas Pipelines, Notice of Proposed Rulemaking, 61 Fed. Reg. 41,046, 41,053-54 (Aug. 7, 1996)).

> FERC's transportation jurisdiction extends as a separate matter over capacity release given the involvement of interstate gas pipelines. The pipelines' role in capacity release is absolutely central, and the transaction itself controls access to interstate transportation capacity . . . .

Pet. App. at 84a-85a (footnotes omitted). Finding "persuasive" this Court's holding in *F.P.C. v. Louisiana Power & Light Co.*, the court of appeals held that FERC's capacity release program is similar to its curtailment regulations[8] in that both involve the pipelines' allocation of transportation capacity among their shippers in compliance with federally mandated strictures. The court of appeals reasoned that because municipalities are subject to the curtailment regulations, they are also subject to FERC's capacity release regulations. Pet. App. at 85a-86a. Indeed, the court of appeals' reasoning is based on the court's analogy of pipeline curtailment plans to capacity release procedures. However, a far more accurate and compelling analogy is that of capacity release to capacity assignment.

Curtailment involves the allocation of a finite resource of interstate pipeline capacity sold in the primary market.[9] In sharp contrast, capacity release involves the ownership, sale, and transfer of pipeline capacity rights by a shipper (here a municipality) in the *secondary market.*[10] Once a municipality

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8. "Curtailment" occurs during periods when the supply of natural gas and/or pipeline capacity falls below contracted-for levels, and the pipelines must redistribute gas supply or capacity to its shippers.

9. The "primary market" is the market in which initial contract rights between the pipeline and the shipper are established.

10. The "secondary market" consists of the transfer of initial contract rights to other shippers.

purchases the pipeline capacity, its handling of its ownership, sale, and transfer rights in such capacity is subject to local regulation.

In contrast to curtailment, capacity release and capacity assignment both deal exclusively with secondary market transactions. In fact, before FERC developed its capacity release program under Order No. 636, FERC had approved "capacity assignment" programs which allowed shippers to assign their firm transportation rights. *Texas Eastern Transmission Corp.*, 51 F.E.R.C. ¶ 61,170 (1990); *Texas Gas Transmission Corp.*, 55 F.E.R.C. ¶ 61,208 (1991); *United Gas Pipe Line Co.*, 46 F.E.R.C. ¶ 61,060, *modified on other grounds*, 49 F.E.R.C. ¶ 61,166 (1989). Although these capacity programs were called "transportation assignment programs," they were the same in concept as the "capacity release" programs established in Order No. 636. For instance, the capacity assignment programs allowed shippers to assign, on any day, all or a portion of their firm transportation capacity rights, and to tender gas for transportation under the shipper's firm service agreement to third parties. *See generally id.*

In explaining its understanding of the transportation assignment program FERC has stated:

> Since the brokering, or assignment, of transportation capacity will control the access to that capacity, the Commission believes that brokering is tantamount to transportation. Therefore, brokering constitutes a new transportation service, subject to the Commission's jurisdiction, that is not covered directly by existing NGA section 7(c) transportation authorizations. The Commission is therefore herein granting

> certificate authorization to persons who are not interstate pipelines.

Texas Eastern Transmission Corp., 51 F.E.R.C. ¶ 61,170 at 61,873 (1990).

The Commission authorized willing persons who were not interstate pipelines to buy, sell, and resell their capacity under firm rate schedules. *Texas Eastern*, 48 F.E.R.C. ¶ 61,248 (1989). As can be seen, these previous capacity assignment programs bear a distinct similarity to the current capacity release program adopted by the Commission in Order No. 636.

A review of FERC's prior decisions regarding capacity assignment readily reveals that the court of appeals' interpretation of *F.P.C. v. Louisiana Power & Light Co.* is fatally flawed. Under *F.P.C. v. Louisiana Power & Light Co.*, the Commission can require a *jurisdictional interstate pipeline* to file a curtailment plan covering gas sold directly to end-users because the Commission has authority over the transportation of such gas. That is true despite the fact that the NGA withheld from the Commission rate-setting authority with respect to direct local sales of natural gas. However, in *Texas Eastern*, 51 F.E.R.C. ¶ 61,170, the Commission soundly rebuffed challenges to its exclusion of *municipalities* from compliance with its regulations with respect to capacity assignment. In doing so, it disposed of the very arguments it now seeks to utilize in Order No. 636 to unlawfully exert jurisdiction over municipalities. The Commission held:

> Anadarko and Process Gas contend that the Commission has jurisdiction over municipalities that assign capacity under the program. Their argument is threefold. First, they argue that the Commission's jurisdiction

> attaches independently to "the transportation of natural gas in interstate commerce." Therefore, the Commission has jurisdiction over any entity that transports gas in interstate commerce. Secondly, they argue that the Commission has the authority under NGA section 7 to condition Texas Eastern's certificate upon the requirement that municipalities comply with all terms and conditions required of other participants. Third, they argue that the Commission has the authority under section 16 of the NGA to require municipalities to obtain and comply with the limited jurisdictional certificates as a prerequisite to program participation.
>
> The August 22 order explains that a municipality is not subject to the Commission's jurisdiction under the NGA because a municipality is not a "person" and therefore cannot be "a natural gas company" under the NGA. 15 U.S.C. §§ 717 (b) and 717 (f). The sections of the NGA to which the intervenors refer apply to "persons." *Since municipalities are not, by definition, persons, the Commission is not persuaded that its interpretation of the NGA is in error.* Accordingly, the request for rehearing on the issue are denied.

Id. at 61,453-54 (emphasis supplied).

FERC went to great lengths in *Texas Eastern* to indicate that, even though the capacity assignment program involved transporting natural gas in interstate commerce, the

municipalities were exempt from conditions imposed upon other participants:

> The August 22 order clarifies that the limited jurisdiction certificates do not apply to municipalities. *The Philadelphia Gas Works requests clarification that all the conditions imposed upon program participants do not apply to municipalities. Since municipalities are beyond the jurisdiction of this Commission, the Philadelphia Gas Works is correct.* The Commission is therefore granting this clarification.

Id. at 61,454 (emphasis supplied).

The court of appeals' ruling permits the Commission to reverse improperly its previous holding, which rejected the notion that municipalities were required to comply with the provisions governing other participants in the capacity assignment program. *Michigan Consolidated Gas Co. v. F.E.R.C.*, 883 F.2d 117, 122 (D.C. Cir. 1989) ("[A]n agency may not casually ignore its own past decisions . . . [but] must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed. . . .") (citations omitted). The court of appeals was obligated to set aside any Commission action that constituted an arbitrary and capricious departure from pre-existing Commission policy without an adequate explanation. *Panhandle Eastern Pipe Line Co. v. F.E.R.C.*, 890 F.2d 435, 439 n.12 (D.C. Cir. 1989). It failed to do so.

Nor is this an isolated FERC decision. In *Panhandle Eastern Pipe Line Co. v. City of Rolla*, 26 F.P.C. 736 (1961), a seminal case that is directly at odds with the court of appeals' holding in *UDC v. F.E.R.C.*, the Commission considered the question of

whether the City of Rolla, a municipality and the co-owner with an interstate pipeline of gas produced and sold in interstate commerce, was a "natural gas company" subject to FERC's NGA jurisdiction. The pipeline disputed the price it was contractually obligated to pay the City of Rolla and sought relief from the Federal Power Commission, FERC's predecessor agency, because sales of gas were then price-regulated under the NGA. The Commission held:

> the plain language of the Act, found in Section 2, subsections (1), (2), (3) and (6) expressly excludes municipalities from the ambit of Commission jurisdiction.
>
> * * *
>
> From this it is clear that municipalities cannot be "natural-gas companies" as that term is used by the Act. We are not, therefore, vested with jurisdiction to regulate municipalities, *even though they are engaged in the sale of natural gas to interstate pipeline companies.* Lacking such jurisdiction, it follows that we are without jurisdiction to resolve disputes between Panhandle and Rolla relating to the contractual price for the sales of gas produced from their jointly owned acreage.

Id. at 737-38 (emphasis supplied).

Similarly, in a 1994 *Tennessee Gas Pipeline Company proceeding*, 69 F.E.R.C. ¶ 61,239 (1994), *on reh'g*, 70 F.E.R.C. ¶ 61,329 (1995), FERC considered whether it could lawfully assert jurisdiction over certain activities of the City of Decatur, Alabama, a municipality as defined in Section 2 of the NGA. In

that case, Decatur had planned to construct substantial pipeline facilities to interconnect with facilities to be constructed by an interstate pipeline. An entity opposing the construction urged the Commission to exercise jurisdiction over the City's proposed facilities, asserting that, under the NGA, the Commission's jurisdiction "attaches independently to . . . the transportation of natural gas in interstate commerce" and that because of the Commission's separate "*transportation*" jurisdiction, FERC must regulate the City's facilities. 69 F.E.R.C. ¶ 61,239 at 61,906-07. FERC flatly rejected this argument. *Id.* at 61,906.

II.

THE COURT OF APPEALS ERRED IN FAILING TO FIND THAT FERC MANIPULATED ITS CAPACITY RELEASE REGULATIONS FOR THE PURPOSE OF CREATING AN IMPROPER JURISDICTIONAL TOEHOLD OVER NON-JURISDICTIONAL MUNICIPALITIES.

The court of appeals recognized that its decision would have been entirely different had it believed that FERC "merely manipulated its regulations" to involve the pipelines in a minimal way in the capacity release program for the purpose of creating a jurisdictional toehold over a nonjurisdictional entity. Pet. App. at 85a, n. 67. Yet, that is precisely what FERC did.

FERC concedes that the pipelines' primary function in these capacity release transactions is that of a "public clearinghouse." Pet. App. at 479a. For example, under the new capacity release programs, the pipeline's primary function is to maintain an electronic bulletin board for shippers desiring to release capacity on which they can post their offers and await other shippers' bids on those offers. Pipelines have no meaningful ability to reject one shipper's offer to release or obtain capacity from another shipper. Accordingly, the new capacity release programs

do not involve the pipelines in any meaningful manner, and they certainly do not have a "central" role such that FERC's jurisdiction would attach.

As noted,[11] despite its similarity to the capacity release program, FERC recognized that municipalities were not subject to the capacity assignment program. The previous capacity assignment program required assignors to notify the pipelines in writing of any assignment of capacity. *Texas Gas Transmission Corp.*, 55 F.E.R.C. ¶ 61,208 (1991). Order No. 636 only minimally changed the requirements to assign, or release, capacity, so as to continue to involve the pipeline in a purely ministerial manner. FERC and the court of appeals interpreted this change as something more, and used this "hook" to expand FERC's jurisdiction to include municipalities. FERC's assertion in Order No. 636-A, that its previous statements of "non-jurisdiction" regarding the mechanics of the capacity release mechanism were not applicable, smacks of jurisdictional overreaching. FERC now suggests that even though the previous transportation assignment program required specific notification to the pipelines of a shipper's actions regarding assigned capacity, the new capacity release regulations include the pipelines in more of the mechanics of the release.[12] This, FERC concludes, allows it to assert jurisdiction over municipalities.

However, absent an act of Congress, FERC cannot assume jurisdiction over municipalities. Given the similarity of the capacity assignment and capacity release programs, the only conclusion one can draw fairly from Order No. 636 is that the agency has manipulated its regulations to create a jurisdictional toehold over non-jurisdictional municipalities.

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11. *See* discussion *supra* at 13-15.

12. Importantly, FERC never explains what it meant by the pipelines' participation in the "mechanics" of the release.

CONCLUSION

For the reasons set forth above, the court of appeals erred in permitting the Commission's unconstitutional assertion of jurisdiction over municipalities, and the petition for a writ of certiorari should be granted.

Respectfully submitted,

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1996

ASSOCIATED GAS DISTRIBUTORS, *et al.*,

Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION and UNITED STATES OF AMERICA,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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BRIEF IN OPPOSITION OF RESPONDENTS PROCESS GAS CONSUMERS GROUP, AMERICAN IRON AND STEEL INSTITUTE AND GEORGIA INDUSTRIAL GROUP

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31pp

QUESTION PRESENTED

Whether the United States Court of Appeals for the District of Columbia Circuit correctly held that the Federal Energy Regulatory Commission ("FERC") did not exceed its jurisdiction under Natural Gas Act Section 1(b), 15 U.S.C.§ 717(b), Pet. App. at 1007a-1008a, to regulate the transportation of natural gas in interstate commerce by requiring the reallocation of interstate pipeline capacity between a local distribution company and its customers, or by a municipality, to comply with FERC's capacity release regulations.

RULE 29.6 LISTING

The Process Gas Consumers Group ("PGC") is an association of industrial consumers of natural gas organized to promote the development and adoption of coordinated, rational and consistent federal and state policies affecting industrial gas users. PGC members own and operate hundreds of manufacturing plants located throughout the United States. PGC has no parent or subsidiary companies.

The American Iron and Steel Institute ("AISI") is the principal trade association of the domestic steel industry. Its 35 domestic members account for approximately two-thirds of the raw steel production capability in the United States. AISI has no parent or subsidiary companies.

The Georgia Industrial Group ("GIG") is an association of industrial users of natural gas located in the states of Georgia and Alabama. GIG actively participates in variety of state and federal proceedings affecting the price of natural gas and electricity in the states of Georgia and Alabama. GIG has no parent or subsidiary companies.

Members of PGC, AISI and GIG consume substantial quantities of natural gas delivered through interstate natural gas pipelines.

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The Process Gas Consumers Group, American Iron & Steel Institute, and the Georgia Industrial Group, Respondents in the captioned cases, respectfully request that this Court deny the petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit (reported at 88 F.3d 1105 (1996)(Pet. App. at 1a to 174a)), submitted by local distribution companies ("LDCs") in No. 96-1186, state regulatory agencies ("PSCs") in No. 96-1188, and municipalities that own local distribution facilities ("municipalities") in 96-1187.

STATEMENT OF THE CASE

The Natural Gas Act ("NGA"), 15 U.S.C. § 717 et seq., provides the basic framework for regulation of the natural gas industry. Since 1978, the regulation of interstate transportation and sales for resale by interstate pipelines has undergone dramatic change. [1]

Regulatory initiatives undertaken by the Federal Energy Regulatory Commission ("FERC") have "unbundled" the sales and transportation services formerly provided in "package" form by interstate pipelines. At the heart of that unbundling is the requirement of "open access" interstate transportation, which is based on the NGA's prohibition against "unduly discriminatory or preferential" rates or terms of pipeline services. 15 U.S.C. §§ 717c(b) and 717d(a). These initiatives

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[1] The court of appeals decision aptly described this regulatory evolution as having "gradually withdrawn from direct regulation of certain industry sectors in favor of a policy of 'light-handed regulation' when market forces make that possible." Pet. App. at 6a. Prior to 1978, producers typically sold gas to federally-regulated, interstate natural gas pipelines who, in turn, provided a combined, or "bundled," transportation/gas sales service to LDCs. The LDCs then provided a state-regulated, bundled retail sales/transportation service to end-users of natural gas.

enable all interested shippers -- including LDCs, end-users, producers and gas marketers -- to contract for interstate transportation of gas among virtually any combination of receipt and delivery points on an interstate pipeline. As a result, LDCs, producers, marketers and end-users are able to sell, buy and ship natural gas virtually anywhere on the interstate transportation grid. A dynamic, integrated national market for natural gas has emerged, complete with a vibrant futures market, actively traded regional markets, and a "secondary market" for interstate transportation rights. At the retail level, many States have implemented similar unbundling programs for LDC sales and transportation services.[2/]

1. The Natural Gas Policy Act of 1978.

Congress took the first step away from the bundled service approach in 1978 by enacting the Natural Gas Policy Act ("NGPA"). 15 U.S.C. § 3301 *et seq.*. The NGPA phased out regulation of wellhead prices charged by natural gas producers. As this Court recently observed, the NGPA also was designed to "promote gas transportation by interstate and intrastate pipelines." *General Motors Corp. v. Tracy*, 1997 U.S. Lexis 692, at *12 (decided February 18, 1997), *quoting* 57 Fed. Reg. 13271 (1992). Thus, with the NGPA, Congress began the process of introducing greater competition into natural gas markets by separating interstate pipelines' sales and transportation functions into discrete services.

2. FERC Order No. 436.

In 1985, FERC sought to further the NGPA's goal of a more competitive national wellhead market by promulgating

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2/ *See generally* U.S. Dept. of Energy, Energy Information Administration, "State Regulators Promote Consumer Choice in Retail Gas Markets," *Natural Gas 1996: Issues and Trends*, at 113-124 (Dec. 1996).

Order No. 436.[3/] In Order No. 436, FERC recognized that encouraging competitive gas markets required nondiscriminatory access to interstate pipeline transportation.[4/] Order No. 436 promoted nondiscriminatory access to the national transportation grid by, among other measures, providing "blanket certificates" (as opposed to the contract-specific, NGA Section 7(c) certificate otherwise required) for pipelines willing to provide transportation service pursuant to open access principles. At their core, these principles required interstate transporters to provide access to all shippers on a nondiscriminatory, "first-come, first-served" basis, even if the shipper intended to compete with the transporter in the sale of gas.[5/] In this way, Order No. 436 sought to afford downstream gas purchasers an alternative to buying gas under pipelines' bundled sales/transportation service.

In the wake of Order No. 436, pipelines sought FERC authorization for a variety of "capacity release,"[6/] "capacity

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3/ *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, FERC Stats. & Regs., Regulations Preambles 1982-1985 ¶ 30,665 (1985)("Order No. 436").

4/ *Id.* at 31,494-504.

5/ *Id.* at 31,516-518. *See Colorado Interstate Gas Co. v. FERC*, 890 F.2d 1121,1123 (D.C. Cir. 1989).

6/ *See, e.g., Arkla Energy Resources*, 53 FERC ¶ 61,127 (1990); *East Tennessee Natural Gas Company*, 53 FERC ¶ 61,304 (1990); *Florida Gas Transmission Co.*, 51 FERC ¶ 61,309, *order on reh'g*, 53 FERC ¶ 61,396 (1990).

brokering"[7] and "transportation assignment" programs.[8] Under such programs, shippers holding interstate pipeline capacity could reallocate their right to use some or all of their pipeline capacity to third-parties. In authorizing capacity brokering and assignment programs, FERC specifically reserved the right to modify or terminate the programs as required by the public convenience and necessity. *See Algonquin Gas Transmission Co.*, 59 FERC ¶ 61,032 at 61,092-93 (1992).[9]

When Congress completed the deregulation of wellhead prices with passage of the Natural Gas Wellhead Decontrol Act

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7/ *See, e.g., Algonquin Gas Transmission Co.*, 53 FERC ¶ 61,417 (1990); *Columbia Gas Transmission Corp.*, 49 FERC ¶ 61,071 (1989); *Kern River Gas Transmission Co.*, 50 FERC ¶ 61,069 (1990).

8/ *See, e.g., CNG Transmission Corp.*, 55 FERC ¶ 61,189 (1991); *Columbia Gas Transmission Corp.*, 49 FERC ¶ 61,071 (1989); *Texas Eastern Transmission Corp.*, 48 FERC ¶ 61,248, *order on reh'g*, 48 FERC ¶ 61,378 (1989), *order on reh'g*, 51 FERC ¶ 61,170, *order on reh'g*, 52 FERC ¶ 61,273 (1990).

9/ Contrary to the PSCs' characterization, FERC did not recognize in *Texas Eastern Transmission Corp.*, 48 FERC ¶ 61,378 at 62,552 (1989)("*Texas Eastern*") that "capacity purchased by LDCs in interstate pipeline facilities should be treated as the LDCs' (not the pipelines') own capacity." PSC Petition at 7. Consistent with "capacity assignment" programs generally, *Texas Eastern* considered reallocation of pipeline capacity held by a second interstate pipeline, Algonquin Gas Transmission Company, not an LDC. Thus, FERC had before it a capacity reallocation issue concerning two entities over which it clearly had jurisdiction; it did not consider whether upstream capacity held by a nonjurisdictional LDC could be considered an "expansion" of that LDC's system. Accordingly, the impression created by the LDCs' replacing the name "Algonquin" with the bracketed words "an LDC's" and "the LDC's" when quoting *Texas Eastern* -- that FERC acknowledged state jurisdiction over interstate capacity held by LDCs -- distorts the meaning of that decision.

of 1989,[10] it urged retention of Order No. 436's "open access" transportation regime. The Congress emphasized that:

> [T]hese new rules, and especially the wide adoption of blanket certificates for nondiscriminatory open access interstate transportation of non-pipeline gas, are essential to its decision to complete the decontrol process.

H.R. Rep. No. 29, 101st Cong., 1st Sess., at 6 (1989). Indeed, Congress encouraged FERC "to retain and improve this competitive structure in order to maximize the benefits of decontrol." *Id.*

3. FERC Order No. 636.

Notwithstanding the partial success of Order No. 436, FERC eventually concluded that shippers purchasing their gas supplies from nonpipeline sources were not receiving the same quality of transportation service as those taking the pipelines' bundled service.[11] This disparity in service quality led FERC to promulgate Order No. 636, which required pipelines

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[10] Pub. L. No. 101-60, 103 Stat. 157 (1989).

[11] *See Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation Under Part 284 of the Commission's Regulations; and Regulations of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 636, FERC Stats. & Regs., Regulations Preambles 1991-1996 ¶ 30,939 at 30,398-407 (Pet. App. at 175a-407a, at 195a-215a), *order on reh'g*, Order No. 636-A, FERC Stats. & Regs., Regulations Preambles 1991-1996 ¶ 30,950 (Pet. App. 408a-812a), *order on reh'g*, Order No. 636-B, 61 FERC ¶ 61,272 (1992)(Pet. App. 813a-998a), *reh'g denied*, Order No. 636-C, 62 FERC ¶ 61,007 (1993)(Pet App. 999a-1000a).

> to provide all transportation services on a basis that is equal in quality for all gas supplies whether purchased from the pipeline or from any other gas supplier.

Order No. 636, Pet. App. at 182a-183a. With Order No. 636, FERC completed its efforts to establish interstate pipeline transportation capacity and natural gas as separate "commodities" obtainable from different sources. Order No. 636 shifted FERC's regulatory focus away from judging the "comparability" of a pipeline's bundled and unbundled transportation services toward

> ensuring that pipeline transportation of all gas supplies is performed on an equal basis under reasonable transportation terms and conditions that enable buyers to use open access transportation to maximize the benefits of a competitive wellhead natural gas market.

Id. at 234a.

As part of Order No. 636's pro-competitive regulatory initiatives, FERC established a framework to govern pipeline customers' reallocation of interstate pipeline transportation capacity to third parties. Previously, FERC had approved differing capacity release, brokering, and reassignment programs for individual pipelines. In Order No. 636, FERC concluded that a structured, industry-wide program permitting "capacity release" would better serve interstate markets than either a prohibition or a collection of individualized programs:

> First, . . . the Commission no longer believes that it can adequately monitor capacity brokering under existing certificates to ensure that all allocations are nondiscriminatory.

> Simply put, there are too many potential assignors of capacity and too many different programs for the Commission to oversee capacity brokering as it now exists. Second, the Commission believes that the two new generic allocation of capacity programs it is adopting make the necessary adjustments to eliminate the potential for firm capacity holders to unduly discriminate in their assignment of capacity, and facilitate the development of the secondary transportation market.

Id. at 238a-239a. Order No. 636's "capacity release" provisions permitted holders of unused interstate pipeline capacity to resell that capacity, either temporarily or permanently, to third-parties through a bidding system maintained by the pipeline. FERC explained that its capacity release mechanism "would afford buyers and sellers of firm capacity with one place to shop to ensure that firm capacity is used as efficiently as possible." *Id.* at 245a.

FERC's capacity release regulations, as supplemented by individual pipelines' tariffs, establish procedures for releasing transportation capacity rights and pipelines' execution of contracts with replacement shippers. Releases may be accomplished through bidding on a pipeline-sponsored electronic bulletin board or through "prearranged releases" negotiated between the releasor and replacement customer or through a combination of those procedures. Ultimately, however, while the terms of the release must be acceptable to the releasor, the terms of the release must also be consistent with the pipelines' filed tariffs and the replacement shipper must enter into a contract with the pipeline to receive the

released transportation service.[12/] Unless the release of capacity is permanent, the releasing shipper would remain liable on its contract with the pipeline, but would receive a credit against its bill for the capacity resold. *Id.* at 245a-252a.

4. The Court of Appeals Decision.

Local distribution companies, PSCs, and municipalities that own local distribution facilities sought judicial review of Order No. 636's capacity release regime. The LDCs challenged certain aspects of FERC's jurisdiction over capacity release transactions (Pet. App. at 79a-80a) and, together with the PSCs, argued that such transactions between LDCs and their customers came within the states' jurisdiction over "local distribution." *Id.* at 81a. The municipalities similarly maintained that their capacity release transactions were outside FERC's jurisdiction because municipalities do not come within the definition of a "natural gas company" subject to the NGA. *Id.* at 83a.

In its decision, the United States Court of Appeals for the District of Columbia Circuit rejected all challenges to FERC's capacity release program. The court of appeals found the release of interstate pipeline capacity to constitute an aspect of the interstate transportation of natural gas. The regulations governing such releases "operate as a term or condition of pipeline service, with which its customers must comply." *Id.* at 80a. Moreover, because this Court's decisions under the Commerce Clause precluded state regulation of interstate transportation, the court of appeals found that

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12/ Pipelines' tariffs permit negotiation of some terms, such as contract duration and, within limits, price. That is, the tariff permits a pipeline to charge rates between a filed maximum and a filed minimum, and neither the pipeline nor the releasor may charge rates outside the FERC-approved range.

> the federal government interceded to ensure stability and protect the interests of the consuming public. It thereby occupied the field, which necessarily includes both the sale and resale of interstate transportation rights.

Id. at 81a. Consequently, the court of appeals concluded that regulation of capacity release transactions fell within the exclusive and plenary jurisdiction over interstate transportation granted FERC under the NGA.

Having concluded that capacity release transactions came within FERC's general jurisdiction over interstate transportation, the court of appeals next declined to adopt the limitations on that jurisdiction proposed by the LDCs, PSCs, and municipalities. The court of appeals found that the jurisdiction over "local distribution" granted states by NGA Section 1(b) "does not withdraw from FERC's jurisdiction any aspect of the interstate transportation of natural gas," *Id.* at 82a, and concluded that "states have never regulated the terms and conditions of interstate pipeline transportation." *Id.*

With regard to the municipalities' definitional argument, the court of appeals reasoned that "FERC's transportation jurisdiction extends as a separate matter over capacity release given the involvement of interstate gas pipelines," *Id.* at 84a, and further observed that "the transaction itself controls access to interstate transportation capacity, entirely independent of the jurisdictional nature of the releasing and replacement shippers." *Id.* at 85a. The court of appeals found "most persuasive" the analogy between FERC's curtailment regulations and the capacity release program, in that "both involve the pipelines' allocation of transportation capacity among their shippers in compliance with federally mandated strictures." *Id.*

REASONS WHY THE PETITIONS SHOULD BE DENIED

I. Petitioners Have Not Demonstrated a Compelling Reason Justifying This Court's Review of the Court of Appeals Decision.

Rule 10 of this Court's Rules instructs that review on a writ of certiorari is not a matter of right, but of judicial discretion, and will be granted only for "compelling reasons." While not an exhaustive listing, Rule 10 identifies reasons that could prove sufficiently compelling to justify the granting of a writ of certiorari. Examples theoretically applicable to the court of appeals decision at issue include conflicting decisions between United States courts of appeals on an important matter, important federal law questions of first impression requiring resolution by this Court, or a court of appeals decision regarding an important federal question that conflicts with relevant decisions of this Court.

Here, the petitions in Nos. 96-1186, 96-1187, and 96-1188 fail to identify a credible, let alone compelling, reason to justify granting a writ of certiorari. The petitions point to the decision of no other circuits with which the court of appeals decision at issue conflicts. The petitions do not purport to identify an important federal question of first impression requiring resolution by this Court. Nor do the petitions demonstrate a conflict between the court of appeals decision and any decision of this Court concerning an important federal question.

The petitions do not challenge the court of appeals' determination that promulgation of the capacity release program represents a permissible exercise of FERC's jurisdiction over the interstate transportation of natural gas. Instead, the petitions argue more narrowly that FERC exceeded

its jurisdiction in applying its capacity release regulations to releases between LDCs and their customers, and by municipalities. According to one petition:

> As should be clear, this petition presents no challenge to the concept of "unbundling" or the overall objectives of the federal plan. Rather, it concerns only the question of ultimate control over one aspect of the current market structure, the resale of capacity by LDCs to in-state customers.

LDC Petition at 24. The petitions disagree at length with the analytical approach adopted by the court of appeals in resolving their jurisdict ional claims, maintaining that inadequate attention was paid to State regulatory prerogatives preserved by the NGA. LDC Petition at 18-20; PSC Petition at 11-13; Municipalities Petition at 9-12.

The petitions fail to identify an "important federal question" warranting this Court's attention. The narrow jurisdictional arguments posited by the PSCs, LDCs and municipalities rest on the fundamental mischaracterization of capacity release transactions between LDCs and their customers, and by municipalities, as "local distribution services" traditionally provided subject to state or local regulation. In fact, the release of interstate pipeline capacity plainly involves interstate transportation by interstate pipelines, not local distribution service -- as the court of appeals correctly found and the petitions do not contest. The released interstate transportation rights extend across many states -- from Texas and Louisiana to New York and Massachusetts and everywhere in between -- and require a contract between the transporting pipeline and the replacement shipper that acquires the service. Indeed, the ability of LDCs and municipalities to release interstate pipeline capacity directly results from FERC's

regulation of interstate pipeline services, including the unbundling of services offered by interstate pipelines. Consequently, as explained in Section II, *infra*, the release of interstate pipeline capacity by LDCs and municipalities, whether to their customers or any other third party, falls within FERC's exclusive jurisdiction over the interstate transportation of natural gas.

Furthermore, while the petitions occasionally reference this Court's precedents regarding the boundaries of federal and state jurisdiction under the NGA, at no time do they identify a single holding of this Court with which the court of appeals decision purportedly conflicts. Indeed, the municipalities' petition attacks the court of appeals for its supposed failure to adhere to *FERC* precedents, not the prior holdings of this Court. *See* Municipalities Petition at 12-19.

At best, the petitions evidence continuing disagreement with the jurisdictional conclusions reached by the court of appeals; however, mere disagreement with the court of appeals, no matter how deeply felt or forcefully expressed, does not justify review by this Court. Thus, the petitions manifestly fail to present a compelling reason for this Court to review the decision of the court of appeals. Accordingly, the petitions for writ of certiorari in Nos. 96-1186, 96-1187, and 96-1188 should be denied.

II. The Court of Appeals Decision Is Consistent with Both the NGA and This Court's Precedents Regarding the Scope of Federal Jurisdiction Over the Transportation of Natural Gas in Interstate Commerce.

The court of appeals decision is entirely consistent with both the NGA and this Court's prior precedents concerning the jurisdictional boundaries between federal and state regulatory

responsibilities. The NGA subjects the natural gas industry "to interlocking regulation by both federal and state authorities." *Northwest Central Pipeline Corp. v. State Corporation Commission of Kansas*, 489 U.S. 493, 506 (1989)("*Northwest*"). The framework for this "interlocking regulation" is set forth in NGA Sections 1(b) and 1(c). *See* 15 U.S.C. §§ 717(b),(c). NGA Section 1(b) provides, in pertinent part, that the statute's provisions "shall apply to the transportation of natural gas in interstate commerce . . . and to natural-gas companies engaged in such transportation." 15 U.S.C. § 717(b). The NGA

> contemplated the exercise of federal power as specified in the Act, particularly in that interstate segment which the states were powerless to regulate because of the Commerce Clause of the Federal Constitution.

FPC v. Panhandle Eastern Pipe Line Co., 337 U.S. 498, 502-503 (1949).

This Court repeatedly has interpreted Section 1(b)'s grant of federal jurisdiction over interstate transportation as affording "exclusive Federal Energy Regulatory Commission jurisdiction over 'the transportation of natural gas in interstate commerce . . . .'" *Northwest*, 489 U.S. at 510. The Court has declared it "well settled" that "Congress occupied the field of matters relating to . . . transportation of natural gas in interstate commerce." *Schneidewind v. ANR Pipeline Co.*, 485 U.S. 293, 305, (1988)("*Schneidewind*"). *See also FPC v. Louisiana Power & Light Co.*, 406 U.S. 621, 636 (1972)("*Louisiana Power & Light*), *quoting Panhandle Eastern Pipe Line Co. v. Public Service Commission of Indiana*, 332 U.S. 507, 516 (1947)(Congress drew three things "within its own regulatory power, delegated by the Act to its agent, the Federal Power Commission" including "the transportation of natural gas in

interstate commerce"); *FPC v. Panhandle Eastern Pipe Line Co.*, 337 U.S. 498, 503 (1949)(same). In so doing, Congress intended that FERC "regulate comprehensively and effectively the transportation and sale of natural gas, and to achieve the uniformity of regulation which was an objective of the Natural Gas Act." *Northern Natural Gas Co. v. State Corporation Commission of Kansas*, 372 U.S. 84, 91-92 (1963)("*Northern Natural Gas*"). *See also Schneidewind*, 485 U.S. at 310 ("uniformity of regulation . . . was an objective of the Natural Gas Act").

This Court has soundly rejected previous attempts to read into NGA Section 1(b) limitations on FERC's plenary jurisdiction over the interstate transportation of natural gas. In *Louisiana Power & Light*, the Court dismissed the contention that federal jurisdiction over transportation applied only to interstate pipeline "sales for resale" and did not reach "direct sales" by interstate pipelines to end-users. The Court explained that each of the areas reserved to federal jurisdiction by Section 1(b)

> is an independent grant of jurisdiction and, though the Act's application to "sales" is limited to sales of interstate gas for resale, the Act applies to interstate "transportation" regardless of whether the gas transported is ultimately sold retail or wholesale.

406 U.S. at 636. Similarly, in *FPC v. East Ohio Gas Co.*, 338 U.S. 464 (1950)("*East Ohio Gas*"), the Court refused to read the federal jurisdiction over interstate transportation as limited to companies that either transported "gas in interstate commerce for hire or for sales to be followed by resales." *Id.* at 468. According to the Court, "the short answer is that the Act's language did not express any such limitation." *Id.* The Court went on to observe that:

> [T]hroughout the Act "transportation" and "sale" are viewed as separate subjects of regulation. They have independent and equally important places in the Act. Thus, to adopt respondents' construction would unduly restrict the Commission's power to carry out one of the major policies of the Act.

Id. [13/]

Contrary to the LDCs' contention that "the perceived federal need for uniformity must give way to the primacy of state regulation as guaranteed by the Act," LDC Petition at 19, this Court has made clear that state regulation may not impinge upon FERC's ability to achieve the comprehensive regulatory scheme mandated by the NGA. Even where a state purports to regulate within a sphere reserved to its jurisdiction by the NGA, "[s]tate regulation . . . may be pre-empted as conflicting with FERC's authority over interstate transportation . . . if state regulation prevents attainment of FERC's goals." *Northwest*, 489 U.S. at 515-16; *Schneidewind*, 485 U.S. at 299-300. For example, in *Northern Natural Gas*, the Court invalidated certain regulatory orders promulgated by the State of Kansas ostensibly pursuant to its NGA Section 1(b) jurisdiction over "production or gathering." Because the orders at issue required an interstate pipeline to purchase gas in a certain manner, the Court concluded that:

13/ NGA Section 1(c), passed by Congress in response to *East Ohio Gas*, does not alter the scope of FERC's jurisdiction over the interstate transportation of natural gas. This Court recently characterized Section 1(c) as simply a Congressional acknowledgement regarding "the important role of the States in regulating *intrastate* transportation and distribution of natural gas." *General Motors Corp. v. Tracy*, 1997 U.S. Lexis 692, *28 (decided February 18, 1997)(emphasis added).

> These State orders necessarily deal with matters which directly affect the ability of the Federal Power Commission to regulate comprehensively and effectively the transportation and sale of natural gas, and to achieve the uniformity which was an objective of the Natural Gas Act. They therefore invalidly invade the federal agency's exclusive domain.

372 U.S. at 91-92. In such situations, the Court emphasized that "[n]ot the federal but the state regulation must be subordinated, when Congress has so plainly occupied the regulatory field." *Id.* at 93. *See also Schneidewind*, 485 U.S. at 310, *quoting Northern Natural Gas*, 372 U.S. at 91-92 ("prospect of interference with the federal regulatory power" permits pre-emption of state law even though "collision between the state and federal regulation may not be an inevitable consequence").

The language of NGA Section 1(b), and this Court's prior decisions interpreting it, make plain that FERC possesses exclusive jurisdiction to regulate a particular *activity, i.e.* transportation of natural gas in interstate commerce. While Section 1(b) also affords FERC jurisdiction over particular entities engaged in such transportation (*i.e.* "natural-gas companies"), this represents a separate jurisdictional grant that does not modify or constrain FERC's Section 1(b) jurisdiction over interstate transportation of natural gas. In other words, FERC's jurisdiction over the interstate transportation of natural gas *is wholly unrelated to the nature of the entities involved in that activity.* For this reason alone, contentions that capacity release transactions between LDCs and their customers, or by municipalities, lie wholly outside FERC's jurisdiction over interstate transportation, are without merit.

Moreover, the NGA's goal of uniform regulation for the interstate transportation of natural gas, together with the states' acknowledged lack of jurisdiction over that activity at the time Congress passed the NGA, further support the conclusion, reflected in the decisions of this Court, that FERC possesses plenary jurisdiction over such interstate transportation. Furthermore, this Court's prior decisions unambiguously instruct that state regulation, *even if nominally within a regulatory sphere reserved to the states by the NGA*, must yield to FERC's jurisdiction if such state regulation would hinder or frustrate FERC's efforts to achieve comprehensive, uniform regulation of interstate transportation.

Here, the court of appeals determined that capacity release transactions were part of an activity -- the interstate transportation of natural gas -- committed to FERC's exclusive jurisdiction by the NGA. Having so found, the court of appeals, in light of the NGA's language and purpose, as well as the prior decisions of this Court, necessarily rejected the contentions, pressed here by the petitions, that the NGA reserved regulation of capacity release transactions between LDCs and their customers, and by municipalities, to state or local authorities. To do otherwise would have opened the door to the regulation of capacity release transactions by multiple state and local regulatory bodies, thereby hindering, if not precluding, FERC's ability to regulate an aspect of interstate transportation -- the reallocation of interstate pipeline capacity -- in the comprehensive, uniform manner intended by the NGA.

Finally, the petitions do not dispute the court of appeals' determination that capacity release transactions are matters subject to FERC's NGA Section 1(b) jurisdiction over interstate transportation. Petitioners' concession on this general jurisdictional determination is fatal to their specific jurisdictional arguments about releases in specific settings. Having conceded that capacity release transactions come within

FERC's exclusive NGA jurisdiction over the interstate transportation of natural gas, Petitioners cannot then credibly argue that the statute simultaneously guarantees "the primacy of state regulation," (LDC Petition at 19) regarding the interstate transportation activities of certain entities (*i.e.*, LDCs and municipalities). Indeed, as noted earlier, the states' *complete lack* of jurisdiction over the interstate transportation of natural gas represented one of the factors necessitating passage of the NGA. If, as the PSCs contend, the NGA intended to reserve to the states "those areas which they had historically controlled," PSC Petition at 11, then Congress could not have reserved to the states the right to regulate an interstate transportation activity such as capacity release because, as the petitions concede, the Commerce Clause denied the States any authority to regulate the transportation of natural gas in interstate commerce. LDC Petition at 4; PSC Petition at 11.

III. The PSC and LDC Petitions Fail to Demonstrate That Capacity Release Transactions Fall Within the States' Jurisdiction Over "Local Distribution."

The petitions submitted by the PSCs and the LDCs make much of the "historic state authority over LDCs and intrastate customers." LDC Petition at 25. *See also* PSC Petition at 14 ("the States long have had power to regulate all aspects of the relationship between LDCs and their end-users"). The PSCs and LDCs contend that, through the jurisdiction reserved to the states by NGA Sections 1(b) and 1(c), Congress intended that states retain "a *comprehensive* scheme of rate control over LDCs." LDC Petition at 24 (emphasis in original). *See also* PSC Petition at 15 ("the state agency has the authority, and a duty, to translate that cost of service into rates that satisfy local concerns"). This comprehensive scheme of state regulation purportedly requires "consistency and exclusivity of control over LDCs' relationship with their local customers"

including the manner in which LDCs reassign their right to use interstate pipeline capacity to those customers. LDC Petition at 24. Otherwise, LDCs might release their interstate pipeline capacity exclusively to out-of-state interests, thereby denying LDC ratepayers the benefit of their "investment" in interstate pipeline capacity. LDC Petition at 27; PSC Petition at 13-14. The PSCs and LDCs characterize FERC's NGA jurisdiction as wholly derivative of and supplemental to the states' jurisdiction. *See, e.g.,* LDC Petition at 19 ("the scope of state authority should have been the touchstone for determining the scope of federal authority"); PSC Petition at 11 (NGA enacted "to fill the gaps in regulatory authority where the States were precluded from acting"). However, whether or not one agrees with the petitioners' policy quarrel with FERC, the petitioners' jurisdictional arguments are baseless.

The interpretation of NGA jurisdiction proffered by the PSCs and LDCs attempts to bootstrap state regulatory authority over rates for "local distribution" into a broader jurisdictional mandate. By framing the crux of their jurisdictional argument in malleable terms such as "the service that LDCs provide to their customers," PSC Petition at 10, and "local distribution companies' services to end-users within the state" LDC Petition at 18, they subtly seek to expand the scope of activities subject to state regulatory authority.

The release of interstate pipeline capacity by an LDC to its customer, however, is not a "service" subject to state jurisdiction for the fundamental reason that it is not a "service" that the states possess authority to regulate on their own. Recall that after issuance of Order No. 436, FERC -- not state regulatory agencies -- authorized pipelines' capacity release, capacity brokering, and capacity reassignment programs. *See supra* notes 6-8.

As the court of appeals correctly determined, capacity release requires either the *temporary or permanent abandonment* of pipeline service to one interstate pipeline customer and the corresponding *initiation of interstate transportation* service to the "replacement" shipper. Pet. App. at 80a. Both abandonment and initiation of interstate transportation service -- the core elements of a capacity release transaction -- are committed to FERC's jurisdiction by NGA Sections 1(b), and are made expressly subject to FERC's approval by NGA Sections 7(b) and 7(c), respectively. 15 U.S.C. §§ 717f(b)(c). For these reasons, plus FERC's exclusive authority over pipelines' tariffs terms and conditions, the court of appeals was correct in concluding that the states "have never regulated the terms and conditions of interstate pipeline transportation." Pet. App. at 82a.

Furthermore, even assuming for argument's sake that FERC's jurisdiction over capacity release transactions was uncertain, the consequences that flow from the state-centric jurisdictional analysis urged by the PSCs and LDCs would necessitate committing those transactions to federal jurisdiction. As this Court explained in *FPC v. Louisiana Power & Light Co*, 406 U.S. 621, 631 (1972):

> [I]n a borderline case where congressional authority is not explicit we must ask whether state authority can predictably regulate a given area and, if we find that it cannot, then we are impelled to decide that federal authority governs.

(*quoting FPC v. Transcontinental Gas Pipe Line Corp.*, 365 U.S. 1, 19-20 (1961)). There, the Court decided that direct sales by interstate pipelines to end-users -- which are not subject to FERC rate regulation -- were subject to FERC's curtailment regulations. In addition to finding curtailment a

matter of interstate transportation, the Court concluded that "[c]omprehensive and equitable curtailment plans for gas transported in interstate commerce . . . are practically beyond the competence of state regulatory agencies." *Louisiana Power & Light*, 406 U.S. at 641. The Court reasoned that:

> the inevitable result would be varied regulatory programs of state courts and agencies, interpreting a countless number of different contracts and applying a variety of state agency rules . . . Besides, a state agency empowered to regulate these contracts would be obliged to regulate in the State, not the national interest.

Id. at 633.

Here, the PSCs and LDCs assert state jurisdictional preeminence over but one aspect of capacity release transactions: releases of interstate transportation made by LDCs to their customers. *See* PSC Petition at 13, 14; LDC Petition at 3, 24. Their petitions do not contend, for example, that releases made by LDCs to entities outside their service territories, or releases obtained by an LDC's end-user customers from an entity other than the LDC, come within a state's regulatory jurisdiction. Thus, even if accepted, the PSCs' and LDCs' jurisdictional claims would leave states without authority to "predictably regulate" all capacity release transactions. Under such circumstances, *Louisiana Power & Light* teaches that extension of state jurisdiction would be unwarranted.[14/]

[14/] This analysis applies with equal force to the municipalities' argument that their capacity release transactions -- but not other capacity release transactions -- are definitionally excluded from FERC's NGA jurisdiction and, therefore, are subject to state or local regulation.

Moreover, partial state jurisdiction over certain capacity release transactions inevitably would bring about the type of cross-cutting, self-interested state regulatory actions eschewed by the Court in *Louisiana Power & Light*. Worse still, the jurisdictional theory espoused by the PSCs and LDCs would produce simultaneous FERC/state regulation of capacity release transactions, the very kind of "overlapping control" that, according to Petitioners, Congress did not intend when it passed the NGA. LDC Petition at 18. *See also* PSC Petition at 14-16 (discussing NGA's "dual jurisdictional design"). If every state could promulgate its own regulations governing LDCs releases of interstate capacity to their own customers, a system of preferences and rates could develop that would interface with interstate transportation access and the federally approved interstate capacity release market. Indeed, the conflicting state and federal regulatory objectives described by the LDCs' petition all but ensure that the dual jurisdiction over capacity releases produced by their interpretation of the NGA would yield regulatory conflict. *See* LDC Petition at 25-28.

Finally, contrary to the PSCs' and LDCs' contentions, FERC's capacity release regulations do not infringe on the states' legitimate ratemaking jurisdiction regarding local distribution service. FERC's regulations establish the maximum rate that can be charged for interstate transportation, including in a capacity release transaction; they do not affect how costs incurred by LDCs are treated for ratemaking purposes at the state level. States' regulatory bodies remain free to allocate the costs of pipeline capacity among LDC customer classes in the manner they deem in the public interest. Equally important, state regulators can (and do) require LDCs to use revenues obtained through capacity releases to reduce the fixed costs borne by the ratepayers whose rates have

"purchased" that interstate pipeline capacity.[15/] In this way, the LDC's ratepayers benefit from its capacity release transactions. Accordingly, claims that ratepayers will lose the benefit of their "investment" in interstate pipeline capacity absent state jurisdiction over LDC capacity release transactions lack substance.

15/ *See, e.g., Re Guidelines for Further Unbundling of Natural Gas,* 148 P.U.R. 4th 441, 444 (N.J. BPU 1993)(directing that the aim of an LDC's capacity release program "should be to provide the greatest contribution to the system's fixed capacity costs, while maintaining reliability for the firm sales customers").

CONCLUSION

For the foregoing reasons, the petitions for writ of certiorari in Nos. 96-1186, 96-1187, and 96-1188 should be denied.

Respectfully submitted,

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In The

Supreme Court of the United States

October Term, 1996

ASSOCIATED GAS DISTRIBUTORS, *et al.*,

Petitioners,

vs.

FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF *AMICI CURIAE* OF THE AMERICAN GAS ASSOCIATION AND CITIZEN ACTION

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for the District of Columbia Circuit

BRIEF *AMICI CURIAE* OF THE AMERICAN GAS ASSOCIATION AND CITIZEN ACTION

Pursuant to Rule 37.2, the American Gas Association (hereafter "A.G.A.")[1] and Citizen Action (hereafter "Citizen") respectfully submit this brief *amici curiae* in support of the petitions for writ of *certiorari* filed by petitioners Associated Gas Distributors, et al., ("AGD") the Public Service Commission for the State of New York, *et al.*, and the American Public Gas Association, *et al.*("APGA"). The written consents of the parties are attached.

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[1] Public Service Company of North Carolina does not join in this brief.

INTEREST OF THE *AMICI CURIAE*

A.G.A. is a national non-profit trade association representing over 200 local distribution companies (hereafter "LDCs" or "gas distributors") principally engaged in distributing natural gas in the 50 states and the District of Columbia. A.G.A. member companies provide retail gas sales and transportation service to more than 55 million residential, commercial and industrial customers across the nation within state designated service territories.

Citizen Action is a nationwide consumer and environmental watchdog organization with over two million members in 31 states. A large percentage of Citizen Action members are residential consumers of natural gas and are concerned about the availability and price of natural gas supplies.

The question presented by AGD and the state commissions is whether the Federal Energy Regulatory Commission ("FERC" or "the Commission") has jurisdiction over LDCs' release to local retail customers of the rights LDCs have purchased to use pipeline capacity to serve local retail sales customers, even though Sections 1(b) and 1(c) of the Natural Gas Act ("NGA" or "the Act")[2] each expressly grant FERC jurisdiction only where states constitutionally cannot act. Similarly, APGA presents the question whether FERC can regulate municipalities' release of pipeline capacity despite the NGA's unequivocal exemption of municipal gas companies from FERC regulation.

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[2] 15 U.S.C. § 717 (b) & (c) (1994) (Pet. App. at 1007a - 1009a).

As national associations of local distributors and gas consumers, A.G.A. and Citizen have a particular interest in the preservation of the statutory prohibition of federal jurisdiction to regulate distribution of natural gas. The opinion of the United States Court of Appeals for the District of Columbia Circuit, affirming the Commission's authority over releases of pipeline capacity rights by LDCs to their retail sales customers, eviscerates the jurisdictional scheme codified by Congress in the NGA by undermining the authority of state regulatory agencies and municipalities to regulate effectively local natural gas distribution companies.

A.G.A. and Citizen accordingly submit this brief *amici curiae* urging the Court to issue its writ of *certiorari* to consider this matter.

SUMMARY OF ARGUMENT

FERC has extended its regulation of open access pipeline transportation to the secondary market in transportation, even under circumstances where LDCs seek to release pipeline capacity rights to their own local retail sales customers for whom they have purchased those rights. Under FERC's rules, unless releases are prearranged at the pipeline's maximum tariff rate or are for a month or less duration, releases of capacity by LDCs must be posted on an electronic bulletin board and are auctioned to the highest bidder, subject to a cap equal to the pipeline's maximum monthly tariff rate. FERC's assertion of jurisdiction over releases of capacity by LDCs to their own retail customers impedes state regulators from ensuring that the local retail customers that pay rates reflecting the full costs of the pipeline capacity in fact gain the benefit of those capacity rights.

LDCs contracted for these capacity rights to provide firm sales service to their local retail sales customers. This retail sales service is subject to the exclusive jurisdiction of the states. Because of FERC's open access pipeline transportation policy, many of these customers now are able to purchase gas from alternative suppliers, but they need to use the pipeline capacity to access alternative suppliers. LDCs and state regulators seek to enable these local retail customers to use the capacity rights the LDC purchased to serve these retail customers through direct releases, unencumbered by FERC's regulation.

FERC's rules interfere with the implementation of state energy policy. FERC's assertion of jurisdiction over capacity releases to local retail customers hampers states in devising optimal mitigation of the firm embedded cost rates paid by LDCs and passed along to firm retail customers. FERC's rules hamper states in crafting programs to enhance local customers' competitive options in the evolving competitive energy markets. The rules interfere with states' ability equitably to allocate the embedded cost of gas transportation to both electricity and gas sold in retail markets.

FERC's regulation, instead, fosters releases of capacity to marketers who often sell to large end-users located out of state. The marketers generally pay only a fraction of the embedded costs of the transportation capacity that are paid by the LDC's residential, small commercial and other firm retail sales customers for whom the capacity is reserved. Thus, the marketers and out-of-state end-users benefit from deep discounts to transportation costs that essentially are paid by the local retail sales customers. In addition, because many

of these out-of-state end-users are electric generators, FERC's rules skew retail energy markets against LDC-supplied gas that bears the full embedded costs of the pipeline's transportation service.

In regulating capacity releases by LDCs to local retail customers, FERC is treading on ground that Congress, in the Natural Gas Act, left to the states to regulate. This Court emphatically and consistently has upheld the principle that the NGA created FERC jurisdiction only over those areas of natural gas transportation and sales that states constitutionally were unable to regulate. Regulation of LDCs' release to local retail customers of transportation capacity purchased to serve those customers is a matter that, under traditional principles of NGA federalism, should be left to the states. FERC has usurped state authority and the court below erred grievously in affirming FERC's decision with respect to this issue.

FERC's rules governing capacity release suffer from the same fatal flaw as the Commission's "Special Marketing Programs" of the mid-1980's, which were remanded by panels of the D.C. Circuit including then Judges Scalia and Ginsburg, in the *Maryland Peoples Counsel v. FERC* cases.[3] The capacity release rules favor large out-of-state end-users, that are not captive to firm gas service, over residential, small commercial and other firm LDC retail customers. These rules stifle development of a robust secondary market in transportation capacity that would benefit all consumers and not just a few favored large volume end-users.

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[3] *Maryland People's Counsel v. Fed. Energy Reg. Comm'n*, 761 F.2d 768 (D.C. Cir. 1985)("MPC I"), 761 F.2d 780 (D.C. Cir. 1985)("MPC II").

ARGUMENT

THE LOWER COURT'S DECISION UNLAWFULLY ALLOWS FERC TO USURP STATE AUTHORITY TO REGULATE NATURAL GAS DISTRIBUTORS' USE OF PIPELINE CAPACITY PURCHASED TO SERVE LOCAL RETAIL CONSUMERS.

A. The Natural Gas Act Preserved the Full Scope of State Regulatory Authority Over LDCs' Activities to Serve Local Retail Consumers and Extended Federal Jurisdiction Only in Areas Where States Constitutionally Cannot Act.

The NGA, 15 U.S.C. §§ 717-717z, conferred upon the Federal Power Commission, precursor to FERC, the power to regulate certain aspects of interstate commerce in natural gas in order to protect the public interest. This Court has confirmed time and again, most recently in *General Motors Corp. v. Tracy,* that Congress intended not to occupy the entire field of its commerce clause power to regulate commerce in natural gas.[4] Rather, Congress intended to occupy only the

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[4] *See General Motors Corp. v. Tracy, Tax Comm'r of Ohio*, No. 95-1232, slip op. at 12 (U.S. Feb. 18, 1997)(stating that the Natural Gas Act left "undisturbed the recognized power of the States to regulate all in-state gas sales directly to consumers"); *Panhandle Eastern Pipe Line Co. v. Public Service Comm'n,* 332 U.S. 507, 516 (1947) (holding that the Natural Gas Act did not preempt state regulation of local direct sales by pipelines to industrial users).

portions of the field not subject to state regulation. The Act expressly provides that federal jurisdiction does not extend to "any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution . . ." 15 U.S.C. § 717(b) (Pet. App. at 1007a - 1008a). *See also* 15 U.S.C. § 717(c) (Pet. App. at 1009a). In upholding the Commission's strained expansion of the NGA, the lower court nullifies the exemption provided by the NGA and thereby allows FERC to intrude into areas Congress expressly left to local control.

LDCs historically purchased bundled service that included gas supplies and firm transportation on interstate pipelines to serve residential, commercial and other retail customers with firm energy needs. Because pipelines now transport for many suppliers, LDCs now manage portfolios of gas supplies they purchase from a variety of sources. LDCs must continue to maintain contracts with pipelines for sufficient firm transportation capacity rights to meet the needs of customers that continue to look to the LDC for reliable gas distribution service, especially on the coldest days of the year.

Under FERC-mandated pipeline rate design, LDCs pay an allocation of the full embedded costs of the pipeline capacity reserved to meet the gas supply needs of their customers. These costs in turn are recovered in the LDC's rates to its firm customers. To mitigate these costs and to enhance efficient use of pipeline capacity, LDCs seek to sell to other shippers transportation capacity rights that the LDCs do not need during any given period. When LDCs transfer these capacity rights directly to their own retail customers, the release should not be subject to FERC's encumbering capacity release program. FERC's assertion of jurisdiction over such direct transfers of capacity rights

to local retail customers precludes states from governing how the value of the capacity purchased incident to retail sales service is allocated among the retail customers that are paying to reserve that capacity. FERC's assertion of jurisdiction here has usurped states' authority to regulate the local economic issues entailed in providing reliable retail gas service.

The decision below affirmed FERC's assertion of jurisdiction over LDCs' release of transportation capacity to local retail customers. In so doing, the court failed to give effect to the full measure of state authority in the area, and instead assumed, contrary to this Court's consistent instruction, that the NGA fully occupied the potential scope of federal jurisdiction.

Petitioners have set forth why federal regulation of LDCs' and municipal utilities' management of the capacity rights they purchase to serve their local sales customers and seek to release to local retail customers exceeds the Commission's authority under the Natural Gas Act. The state commissions' petition describes how FERC's regulation impedes states' rights effectively to protect the economic interests of the captive retail consumers of natural gas. A.G.A. supports but will not repeat these arguments; instead we describe how the Commission's regulation has the perverse effect of penalizing precisely the natural gas consumers that the NGA is intended to protect.

B. Competition and Open Access Unbundled Transportation Fundamentally Have Altered Commercial Relationships in Natural Gas Markets, But NGA Jurisdiction Remains Circumscribed by State Authority to Regulate Commerce in the Interests of Local Retail Consumers.

To foster a more competitive natural gas market, Congress passed the Natural Gas Policy Act of 1978 ("NGPA") which removed "first" sales (usually by producers) of natural gas from FERC jurisdiction under the NGA.[4] A competitive spot market in natural gas developed along with a gas futures market to support it. But the wellhead market continued to remain dominated by pipeline purchasers of gas because other purchasers had no meaningful access to the pipeline transportation systems essential to reach consumers. FERC's initial "experimental increase in [natural gas] pipeline competition" was rejected as too narrow by the D.C. Circuit in the *Maryland Peoples Counsel* cases.[5] In those cases, panels led by then Judges Scalia and Ginsburg remanded FERC's "Special Marketing Programs" that had favored industrial end-users of natural gas at the expense of residential and small commercial consumers and thereby harmed rather than helped "the consumers whom the Natural Gas Act was

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[4] 15 U.S.C. §§ 3301 - 3348 (1994).

[5] 761 F.2d 768, 770 (brackets in original); *see also* 761 F.2d 780, 781 ("[t]his case features [FERC] blanket permission for interstate transportation of natural gas sold directly by producers to end users").

designed to protect." MPC II, 761 F.2d at 781 (internal quotations omitted).

In part responding to these cases, the Commission promulgated rules providing for non-discriminatory, "open access" transportation of gas by pipelines,[6] culminating in the Order No. 636 series, reviewed and remanded in part by the opinion below.[7] Briefly, Order No. 636 prohibited pipelines from selling the commodity gas bundled under a single price with the transportation service required to deliver the gas to the LDC buyer. Instead, Order No. 636 required pipelines to offer all transportation and storage services separately from the commodity, on an "open access" basis to all shippers, including those that buy gas from the pipeline (or the pipeline's marketing affiliate), under nondiscriminatory terms and conditions. The goal of requiring "open-access" transportation unbundled from the gas sale itself, the Commission said, was to "maximize the consumer benefits of the competitive

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[6] *See General Motors,* slip op at 13-14; s*ee also* Richard J. Pierce, "The Evolution of Natural Gas Regulatory Policy," Nat. Resources and Env't L.J., Summer 1995 at 53 (providing an overview of the history of natural gas regulation).

[7] Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulations of Natural Gas Pipelines After Partial Wellhead Decontrol, 57 Fed. Reg. 13267, III FERC Stats. & Regs. Preambles ¶ 30,939 (1992) ("Order No. 636") (Pet. App. at 175a - 407a); *Order on Reh'g*, 57 Fed. Reg. 36128, III FERC Stats. & Regs. ¶ 30,950 ("Order No. 636-A) (Pet. App. at 408a - 812a) *Order on Reh'g*, 57 Fed. Reg. 57911, 61 FERC ¶ 61,272 (1992) ("Order No. 636-B") (Pet. App. at 813 a - 998a); *Reh'g Denied*, 62 FERC ¶ 61,007 (1993) ("Order No. 636-C) (Pet. App. at 999a - 1000a), upheld in part and remanded in part, *United Distribution Cos. v. Federal Energy Regulatory Comm'n,* 88 F.3d 1105 (D.C. Cir. 1996) (Pet. App. at 1a - 174a); o*rder on remand*, 78 FERC ¶ 61,186 (Feb. 27, 1996).

wellhead gas market" by ensuring "that all shippers have meaningful access to the pipeline transportation grid so that willing buyers can meet in a competitive, national market to transact the most efficient deals possible."[8]

The Commission's rules requiring open access transportation and unbundling of the commodity sale from the transportation service allowed the development of a free and open wellhead market in gas commodity sales so that a multiplicity of suppliers could flourish by accessing the robust market of consumers. Now gas markets are at the next step where a robust and resilient secondary market for transportation should develop to maximize efficiency and to enable the benefits of competition to accrue directly to all consumers, not principally to large industrial or electric companies. But FERC's assertion of authority over LDC releases of capacity to local retail customers, like its "Special Marketing Programs," favors large out-of-state end-users who do not need firm LDC service and harms the residential, small commercial and other consumers that need firm supplies and pay for the reserved capacity. The capacity release regulation itself thereby undermines the goal of maximizing the consumer benefits of competition and FERC commits the same error found in the *Maryland People's Counsel* cases.

Under state regulation, LDCs also are instituting a variety of unbundled services for retail customers, enhancing the flexibility of end-users of natural gas to access directly gas being sold in competitive markets. LDCs now routinely serve retail customers that choose to purchase gas from alternative gas suppliers by assisting in arranging for pipeline transportation services

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[8] Order No. 636, 57 Fed. Reg. at 13281 (Pet. App. at 234a).

and combining those pipeline services with transportation and delivery services on an LDC's system.[9] In many states, LDCs also are offering services such as storage, balancing and standby gas sales on an unbundled basis.[10]

This Court pointed out in *General Motors*, slip op. at 24, that residential and small commercial customers still rely on transportation, distribution and sales service from LDCs bundled together to meet consumers' basic energy requirements, such as space heating.[11] This Court further emphasized that utilities have an *obligation* under state laws to serve these customers' demand. *Id.* at 17-18 & n. 10. LDCs therefore must contract for a sufficient firm daily supply of gas and pipeline delivery capacity to satisfy potential "peak day" needs of these customers, *i.e.* the higher level demand for gas service that occurs when the weather is coldest, even though average daily needs

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[9] In fact, 81 percent of gas used by industrial customers is purchased from suppliers other than their LDCs, and 25 percent of gas used by commercial customers is purchased from alternative suppliers. Dep't of Energy, Energy Info. Admin., Natural Gas Monthly, Table 24 "Percentage of Total Deliveries Represented by Onsystem Sales, by State, 1994-1995," Jan. 1997 at 64.

[10] *See generally* American Gas Association, "Gas Distribution Industry Pricing Strategies 1995 Update," (FA95-2, Dec. 1995); American Gas Association, "Providing Unbundled Services to Small Volume Customers: Issues to Consider in the Implementation Process," (IB 1996-02, January 5, 1996); American Gas Association, "Providing New Services to Residential Customers: A Summary of Pilot Programs and Unbundling Initiatives," (IB 1996-11, 11A, 11B, 1996).

[11] In addition, certain large customers, such as some apartment buildings, hospitals, industrial plants, etc. continue to prefer firm LDC service.

typically are substantially lower than the potential peak day.[12]

FERC regulates pipeline rates for firm capacity, *i.e.*, capacity that is not subject to interruption, and generally designs firm rates so that all of the fixed costs of the pipeline facilities and business during the course of the year are recovered in the charges that are prorated and paid monthly by the firm customers regardless of how much gas they require to be delivered through the capacity they have reserved. LDCs' rates recover the costs an LDC must pay a pipeline for reserved capacity along with the costs of local delivery facilities and other expenses they incur to serve their customers. State commissions actively oversee these costs to ensure that LDCs are prudent in managing their resources to provide reliable service without overpaying for gas supplies or using pipelines' transportation capacity in an uneconomic manner.[13]

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[12] In fact a typical residential load factor is only 25%; that is, on an average annual basis, residential customers take only 25% of the gas, or use only 25% of the capacity, that they require on peak and are entitled to take.

[13] *Cf. Pike County Light & Power Co. v. Pennsylvania Public Utility Comm'n*, 77 Pa. Commw. 268, 273-274, 465 A.2d 735, 737-738 (1983) (while states cannot bar regulated utilities from passing through to consumers FERC-approved wholesale rates, states properly review the prudence of LDCs' decisions to incur those costs that are avoidable or discretionary); *Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354, 385 (1988)(Brennan, J., dissenting).

C. Including LDCs' Release of Capacity to Local Retail Customers Under FERC's Rule Results in Subsidies to Large Users and Marketers from Consumers That the NGA was Intended to Protect.

Order No. 636 permits LDCs and other holders of firm pipeline capacity to "release" pipeline capacity that currently is not being used to meet customer demand; that is, LDCs may allow third parties to use the capacity when the LDCs are not using it themselves to ship gas.[14] As defined by FERC, capacity release is the "reallocat[ion] [of] unneeded firm capacity" on a permanent or temporary basis.[15]

FERC's rules prescribe a number of cumbersome administrative procedures that not only impede LDCs' ability to use their firm rights to capacity for the benefit of their firm core customers, but also usurp states' efforts to assure the maximum benefit for the LDC customers that need and pay for the firm capacity. First, the capacity must be posted on the pipeline's Electronic Bulletin Board in a certain format and with comprehensive information. Second, the capacity must be sold to the highest bidder at a public

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[14] Order No. 636, 57 Fed. Reg. at 13824 (Pet. App. at 245a).

[15] *Id.* at 244a.

auction, subject to a rate cap equal to the pipeline's maximum approved monthly tariff rate.[16] The replacement shipper contracts directly with the pipeline, and pays the pipeline for the transportation service. The pipeline then credits the releasing LDC with the revenues from the new shipper. The LDC releasing the capacity remains obligated to the pipeline for the difference between the release price and the contract demand charge.[17]

Gas marketers won 79 percent of the capacity release awards during 1995 and that number is growing.[18] Marketers combine the released capacity with gas supplies and sell a bundled service to end-users that often are located in other states. The result is that the released capacity -- which was reserved for the use and benefit of the LDC's retail customers -- goes to other parties who do not carry the economic cost of reserving that capacity.

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16 FERC created two exceptions to the bidding process: 1) if the capacity release was prearranged at the maximum pipeline tariff rate and 2) if the capacity was released for one month or less. 18 C.F.R. §284.243(e) & (h), Order No. 636-A, 57 Fed. Reg. at 36145-46 (Pet. App. at 481a - 485a). Capacity released under these two exceptions to bidding remains subject to the Commission's rate cap. An LDC retail customer may match the highest bid and win the capacity but this is no remedy to the interference by misplaced federal regulation in state programs to enhance competitive purchase opportunities and efficient capacity allocations in local retail markets.

17 Order No. 636, 57 Fed. Reg. at 13284 (Pet. App. at 246a).

18 *See* Interstate Natural Gas Association of America, "Gas Transportation Through 1995," Issue Analysis, Rept. No. 96-3, Sept. 1996 at 8.

The economic harm to the retail customers caused by FERC's rule does not stop there. During most of the year, including the transition months of Spring and Fall, the average rates for released capacity are significantly below the maximum interstate pipeline tariff rates, and therefore significantly below a ratable share of the cost of providing the transportation service. Over the entire 1995-96 winter heating season, which was colder than normal, rates for released capacity nonetheless were discounted an average of 65 percent below maximum tariff rates.[19] During the non-heating season, April through October, capacity release rates were discounted 83 percent.[20] The economic benefit of these deep discounts often goes to the out-of-state dual fuel large users of natural gas or to the marketers serving them, depending upon market conditions.

FERC's rule perpetrates further economic harm to the retail customers who reserve and pay for firm capacity. During the coldest days of the winter, the market value of the released capacity may exceed the maximum approved tariff rate of the pipeline. FERC's monthly rate cap, however, precludes LDCs from recovering the true market value of the capacity to the detriment of the retail customers. The market value of pipeline capacity can be derived from comparing the price of gas in the production area with the price of gas at a particular city gate in markets that are distant from production. For example, in December 1996, the average spot price for gas purchased in Louisiana, a

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19 Dep't of Energy, Energy Info. Admin., *Natural Gas 1996: Issues and Trends,* December 1996, at 46-47.

20 *Id.*

major supply area, was $3.84 per MMBtu while the average spot price for gas purchased at the New York city gate was $5.22 per MMBtu.[21] The $1.38 difference between the purchase price in Louisiana and the purchase price in New York includes approximately $.24 associated with fuel, and other add-ons that are not part of the value of the transportation. Subtracting these costs leaves $1.14 as the value of the transportation from Louisiana to New York.

Under FERC's rules, however, LDCs may charge no more than the pipeline's maximum tariff rate for released capacity. A typical maximum transportation rate on a major interstate pipeline that extends from Louisiana to New York City is approximately $.31 per MMBtu. Thus the mitigation of the embedded costs paid by the LDCs' sales customers was limited to $.31, while the marketer was able to net an additional $.83 per MMBtu.

Under state law, state regulators are charged with protecting the public interest in energy services at reasonable prices. These matters clearly encompass allocating the value of capacity rights purchased by retail customers -- without interference by FERC regulation. Had FERC not usurped state regulation of capacity reserved for retail sales, the $.83 difference between the maximum tariff rate and the true value of the capacity rights would have been available to mitigate the cost to the in-state customers who paid for the capacity year round if the state so elected. The state could have elected to impose an *annual* revenue cap for released capacity equal to the pipeline's annualized embedded cost rate. State energy policy should govern

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[21] Brent Friedenberg Assocs., Ltd., *U.S. Northeast Natural Gas Market Review*, December 1996, Table C1, at 28.

allocation of the economic benefit, as well as the capacity itself, that was reserved for local retail sales is resold to local retail customers.

A significant percentage of the out-of-state, large dual-fuel users of released capacity are electric generators. Thus FERC's rule results in subsidies from LDC firm gas sales customers to electric generators. A federal regulation that indirectly requires local gas consumers to subsidize costs of generating electricity wreaks havoc with state efforts to avoid cross subsidies among fuels and is a serious encroachment into the state regulatory domain of integrated resource planning. Moreover, to the extent electric generators using released capacity pay below embedded costs for transportation, LDCs are disadvantaged in competing in retail energy markets because retail gas rates must reflect the share of pipeline embedded costs that electric generators are not paying.

D. States Constitutionally Can Regulate Unbundled Retail Transportation Services and the NGA Left That Authority Undisturbed.

This Court emphatically has defended the breadth of states' authority to regulate public utilities' service to local retail customers against efforts to read the Natural Gas Act as diminishing that authority. Paraphrasing *Panhandle,* 332 U.S. 507, the Court in *General Motors* said:

> Congress's purpose in enacting the NGA was to fill the regulatory void. . . the NGA "was drawn with meticulous regard for the continued exercise of state power, not to handicap or dilute it in any

> way [T]he scheme was one of cooperative action between federal and state agencies. . . and Congress' action . . . was an unequivocal recognition of the vital interests of the states and their people, consumers and industry alike, in the regulation of rates and service." [Citations omitted.]

General Motors, slip op. at 12 (quoting *Panhandle v. Public Service Comm'n,* 370 U.S. at 519-522).

Historically, LDCs' use of pipeline capacity incident to serving their local retail customers has been subject to strict oversight by state regulatory agencies. The sale by LDCs of transportation capacity rights, separate from the sale of natural gas itself, at the retail level does not change the local nature of the overall transaction -- natural gas service to consumers. Local retail gas service involves issues of critical importance to states, such as adequate supplies and reliable delivery capacity so that consumers are not cut off in cold weather, as well as impacts on the local economy. Congress in the NGA has left those issues to the states and the Court below erred in affirming FERC's preemption of state authority.

LDCs should be permitted to release capacity to customers behind the city gate under terms regulated by the states for the benefit of those customers on behalf of which the LDC reserved the firm capacity and is paying the full embedded costs. Congress in the NGA left to state regulation that which the constitution permits states to regulate. The disposition of rights to move gas to local end-user markets is an area of local concern constitutionally within the states' purview.

CONCLUSION

For the reasons stated, A.G.A. and Citizen urge the Court to grant the petitions for a writ of *certiorari* to the D.C. Circuit in Nos. 96-1186, 96-1187, and 96-1188.

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Nos. 96-1186, 96-1187, 96-1188 and 96-1189

In the Supreme Court of the United States

OCTOBER TERM, 1996

ASSOCIATED GAS DISTRIBUTORS, ET AL., PETITIONERS
v.
FEDERAL ENERGY REGULATORY COMMISSION

AMERICAN PUBLIC GAS ASSOCIATION AND CITIZENS GAS & COKE UTILITY, PETITIONERS
v.
FEDERAL ENERGY REGULATORY COMMISSION

NEW YORK PUBLIC SERVICE COMMISSION, ET AL., PETITIONER
v.
FEDERAL ENERGY REGULATORY COMMISSION AND UNITED STATES OF AMERICA

BURLINGTON RESOURCES OIL & GAS COMPANY, PETITIONER
v.
FEDERAL ENERGY REGULATORY COMMISSION

ON PETITIONS FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

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QUESTIONS PRESENTED

Order No. 636 of the Federal Energy Regulatory Commission (FERC) requires the unbundling of interstate natural gas transportation service from sales service in order to facilitate competition in the national market for gas at the wellhead and ensure equal access to transportation services. The questions presented are:

1. Whether FERC's jurisdiction over interstate transportation of natural gas under the Natural Gas Act, 15 U.S.C. 717 *et seq.*, supports application to local natural gas distribution companies and municipally owned natural gas companies of FERC regulations governing transfer of rights to capacity on interstate natural gas pipelines.

2. Whether FERC correctly concluded that, pursuant to its program for reallocation of pipeline capacity under long-term transportation contracts, it could not require natural gas pipelines to accept bids lower than the maximum just and reasonable rate for transportation capacity.

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In the Supreme Court of the United States

OCTOBER TERM, 1996

No. 96-1186

ASSOCIATED GAS DISTRIBUTORS, ET AL., PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION

No. 96-1187

AMERICAN PUBLIC GAS ASSOCIATION AND CITIZENS GAS AND COKE UTILITY, PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION

No. 96-1188

NEW YORK PUBLIC SERVICE COMMISSION, ET AL., PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION AND UNITED STATES OF AMERICA

No. 96-1189

BURLINGTON RESOURCES OIL & GAS COMPANY, PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-174a)[1] is reported at 88 F.3d 1105. The orders of the Commission are reported in Order No. 636, *Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation Under Pt. 284 of the Commission's Regulations, and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, F.E.R.C. Stats. & Regs. (CCH) ¶ 30,939 (Pet. App. 175a-407a), order on reh'g, Order No. 636-A, F.E.R.C. Stats. & Regs. (CCH) ¶ 30,950 (Pet. App. 408a-812a), order on reh'g, Order No. 636-B, 61 F.E.R.C. (CCH) ¶ 61,272 (Pet. App. 813a-998a), reh'g denied, 62 F.E.R.C. (CCH) ¶ 61,007 (Pet. App. 999a-1000a) (Order No. 636).

JURISDICTION

The judgment of the court of appeals was entered on July 16, 1996. A petition for rehearing was denied on October 29, 1996. Pet. App. 1003a-1004a. The petitions for a writ of certiorari were filed on January 27, 1997. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. In the rule at issue here, Order No. 636, the Federal Energy Regulatory Commission (FERC or Commission) completed the natural gas deregulatory program it had initiated almost a decade earlier. Order No. 636 mandates the "unbundling" of interstate natural gas sales service from transportation service, requiring that those services be sold separately to

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[1] All references to "Pet. App." are to the appendix to the petition in No. 96-1186.

natural gas purchasers. FERC adopted its mandatory unbundling policy in order to "improve the competitive structure of the natural gas industry to facilitate the operation of a national wellhead market as envisioned by Congress," Pet. App. 229a; to "ensure equality of transportation service between gas sold by pipelines or their affiliates and gas sold by other sellers," *id.* at 234a; and, ultimately, to "provide natural gas consumers with access to an adequate supply of clean and abundant natural gas at reasonable prices," *id.* at 229a. Order No. 636 imposes "capacity-release" requirements that allow holders of firm transportation rights on interstate pipelines to resell those rights under uniform terms. *Id.* at 244a-252a.[2] The order also imposes right-of-first refusal (ROFR) requirements, which allow existing shippers with long-term transportation contracts to retain their rights to pipeline capacity if they agree to match the highest bid for that service from alternative purchasers, up to the maximum cost-based transportation rate for the service approved by the Commission under the Natural Gas Act (NGA), 15 U.S.C. 717 *et seq.* Pet. App. 671a-692a.

2. In 1985, FERC initiated a deregulatory program designed to encourage the voluntary unbundling of pipeline gas sales from pipeline transportation services. Whereas pipelines had traditionally bought gas at the wellhead and transported it before turning it over to the purchaser, the Commission dramatically

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[2] Transportation is referred to as "firm" when delivery is guaranteed without interruption, as distinguished from "interruptible" transportation, which may be interrupted to accommodate the requirements of firm shippers. See Pet. App. 11a n.10.

changed the natural gas industry by enabling pipelines to offer gas sales and transportation services separately, thereby affording customers the opportunity to purchase gas from one company and hire a separate company's pipeline to transport it. See Pet. App. 10a-15a (discussing background to Order No. 636). To further enhance the efficiency of the natural gas market, the Commission encouraged pipeline customers, through a variety of mechanisms, to sell or release their unwanted firm transportation capacity to other shippers.

The partial unbundling of sales and transportation service that resulted from the voluntary program presented serious inefficiencies in allocation of unused transportation capacity. For example, because bundled firm service had often provided superior reliability, many customers continued to pay reservation fees to retain that service, while in most instances using cheaper interruptible service to transport their wellhead gas. See Pet. App. 15a-16a. The secondary transportation market that resulted from partial unbundling produced such a wide variety of capacity-reallocation arrangements that it became impossible for FERC to monitor those programs adequately in order to "ensure that all allocations are nondiscriminatory"; there were "simply too many potential assignors of capacity" for FERC to assure that capacity was allocated "in a manner consistent with the public convenience and necessity." *Algonquin Gas Transmission Co.*, 59 F.E.R.C. (CCH) ¶ 61,032, at 61,095 (Apr. 8, 1992), reh'g denied, 60 F.E.R.C. (CCH) ¶ 61,113 (Aug. 3, 1992).[3] Accordingly, the Commission

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[3] In the *Algonquin* orders, which were issued as companion orders to Order No. 636, the Commission revoked the certifi-

found that the continued operation of the voluntary capacity reallocation programs it had previously approved "would frustrate the goal of * * * remedy[ing] an unreasonable restraint of trade" and would therefore be "unjust and unreasonable and contrary to the public interest." 59 F.E.R.C. (CCH) ¶ 61,032, at 61,096-61,097.

3. To address the problems that arose from partial, voluntary unbundling, FERC's Order No. 636 mandates the complete unbundling of pipeline sales from transportation service and institutes a number of requirements to achieve a fair and open market for transportation rights, and to prevent undue discrimination. See Pet. App. 15a-18a (summarizing Order No. 636).

FERC established, *inter alia*, a uniform capacity-release rule to ensure that unneeded transportation capacity on interstate pipelines is allocated fairly and efficiently. See Pet. App. 71a-103a, as amended by Pet. App. 1001a-1002a, 244a-252a.[4] Under FERC's rule, any shipper desiring to release firm capacity must notify the affected interstate pipeline. The pipeline must then post the available capacity, along with applicable conditions, on an electronic bulletin board for a reasonable period of time, and assign the capacity to the shipper making the best offer for the capacity, up to the maximum just and reasonable price established by the Commission. *Id.* at 245a-247a. A

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cates of public convenience and necessity it had previously issued for capacity reallocation programs and required instead that pipelines abide by the uniform capacity reallocation program of Order No. 636. Review of those orders was consolidated with review of Order No. 636. Pet. App. 19a & n.20.

[4] FERC's capacity-release rule is codified at 18 C.F.R. 284.243.

shipper releasing firm capacity transportation rights may designate a specific party to receive those rights, but the pipeline must post such a prearrangement on the electronic bulletin board, and the designated party can receive the transfer only if no other party makes a better offer. *Id.* at 244a-247a. If the designated shipper bids at the ceiling rate, however, it automatically receives the transportation rights. *Id.* at 245a.

In addition, FERC recognized that, if the wellhead market for natural gas is to function effectively, transportation should be made equally available to all gas purchasers, regardless of whether the wellhead merchant is affiliated with the pipeline. Pet. App. 234a-235a. The principle of "transportation equality" protects captive customers—*i.e.* those connected to only one pipeline, who typically have long-term contracts—from the pipeline's market power. To implement that principle, Order No. 636 imposes, *inter alia*, a "right-of-first-refusal" (ROFR) process allowing competitive allocation of capacity at the expiration of long-term contracts for pipeline transportation, while protecting customers with expiring contracts who remain dependent upon continued transportation service. See *id.* at 43a-56a.

As a condition of granting pipelines authority, under Section 7(b) of the NGA, 15 U.S.C. 717f(b), to abandon contracts at the end of their terms, FERC required pipelines to institute a ROFR mechanism inviting renewal of any long-term contract if the existing shipper matches the highest offer (up to a maximum just and reasonable rate) from any competing bidder for the transportation capacity. 18 C.F.R.

284.221(d); Pet. App. 668a-673a.[5] FERC reasoned that, in general, "a pipeline's service obligation * * * should be determined, in the first instance, by the contract negotiated by the parties," *id.* at 312a, and pipeline transportation capacity is most efficiently allocated if it is sold to those willing to pay the highest price for the capacity, *id.* at 675a. The Commission recognized, however, that where contracts for longer than one year are involved, existing customers may rely on continued service and require some assurance that their current long-term contracts can be extended.

The Commission concluded that the ROFR mechanism "strikes the appropriate balance between the needs of customers for continued service and the benefits of competition in establishing the terms of service." Pet. App. 325a.

4. The court of appeals upheld in large part FERC's Order No. 636, remanding only issues not relevant here. The court concluded that FERC's plenary jurisdiction over interstate transportation of gas on interstate pipelines gives it the authority to regulate the exchange of interstate transportation capacity. Pet. App. 71a-94a. Uniform capacity-release requirements "operate as a term or condition of pipeline service" that FERC may apply to all parties engaged in such interstate transactions, including parties that otherwise are exempt from FERC jurisdiction as local distribution companies (LDCs)

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[5] A pipeline must also extend a contract if it contains either an evergreen or a rollover clause. Such clauses allow parties to extend their contract for a specified term upon the contract's expiration. See Howard R. Williams, *Manual of Oil & Gas Terms* 406-407, 1083-1084 (8th ed. 1991).

or municipally-owned natural gas distributors (municipals). *Id.* at 80a. The court rejected petitioners' asserted distinction between "rights to" and "rendition of" service, concluding that, "[w]hile the pipeline provides *transportation* only when a party utilizes capacity rights to transport gas, the pipeline provides *transportation services* throughout the capacity release process." *Ibid.* (emphasis in original).

The court also rejected several challenges to the ROFR mechanism. Pet. App. 43a-56a.[6] The court upheld the Commission's conclusion that it could not require pipelines considering existing customers' bids under the ROFR mechanism to accept rates below the maximum just and reasonable rate. *Id.* at 53a-56a. The court also concluded that the Commission had included adequate safeguards in Order No. 636 against pipeline manipulation of bids, that there was no basis upon which to require pipelines to accept bids at less than the approved rate, and that the Commission had provided proper incentives in the ROFR process to encourage pipelines to accept discounted rates. *Ibid.*

ARGUMENT

Petitioners challenge the court of appeals' decision upholding the capacity-release and ROFR requirements of Order No. 636. That decision is consistent with the well established principle that the NGA

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[6] Although the court generally affirmed the Commission's ROFR mechanism, it remanded for further consideration the requirement that, in order to retain their existing pipeline capacity, existing shippers must match bids for terms of up to 20 years duration. Pet. App. 49a-53a. On remand, the Commission shortened the maximum term to five years. Order No. 636-C, 78 F.E.R.C. (CCH) ¶ 61,186 (Feb. 27, 1997).

granted FERC "exclusive jurisdiction 'over the sale and transportation of natural gas in interstate commerce,'" *Northwest Cent. Pipeline Corp.* v. *State Corp. Comm'n*, 489 U.S. 493, 510 (1989), and with the decisions of this and other courts construing that grant of jurisdiction. Further review is not warranted.[7]

1. Petitioners Associated Gas Distributors, et al. (AGD) (No. 96-1186), the New York Public Service Commission, et al. (NYPSC) (No. 96-1188) and the American Public Gas Association, et. al. (APGA) (No. 96-1187) challenge the court's affirmance of the capacity-release requirements in Order No. 636. The court of appeals correctly concluded that FERC's capacity-release program is a legitimate exercise of its plenary jurisdiction under the NGA to regulate the transportation of gas in interstate commerce.

a. There is no merit to petitioners' contentions (96-1186 Pet. 18-24; 96-1188 Pet. 13-16) that the Com-

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[7] Order No. 636 comports with FERC's obligation under the NGA to ensure consumers a supply of gas "at the lowest possible reasonable rate." *Atlantic Ref. Co.* v. *Public Serv. Comm'n*, 360 U.S. 378, 388 (1959). As recent studies demonstrate, consumers have reaped substantial benefits from the Commission's decade-long restructuring of the natural gas industry, of which Order No. 636 represents the "latest step." Pet. App. 6a. Specifically, adjusted for inflation, prices paid by local utilities for gas at the "city gate" dropped by 52% in the last decade, prices paid by residential and commercial customers dropped 32% and 38%, respectively, and prices paid by industrial and electric utility customers fell by approximately 60%. Those figures demonstrate that "open access has placed strong pressures on interstate pipelines to reduce their costs and pass the savings through to their customers." Robert Crandall & Jerry Ellig, *Economic Deregulation and Customer Choice: Lessons for the Electric Industry* 10-11 (1997).

mission lacks jurisdiction to apply its capacity-release rules to capacity on interstate pipelines held by LDCs. As the court of appeals concluded, "FERC's capacity release program is a legitimate exercise of its jurisdiction over the interstate transportation of natural gas." Pet. App. 77a. Section 1(b) of the NGA grants the Commission jurisdiction over three distinct aspects of the natural gas industry: (1) "the transportation of natural gas in interstate commerce," (2) "the sale in interstate commerce of natural gas for resale for ultimate public consumption," and (3) "natural-gas companies engaged in such transportation or sale." 15 U.S.C. 717(b); see *FPC* v. *Louisiana Power & Light Co.*, 406 U.S. 621, 636 (1972) (*LP&L*). As this Court has emphasized, the Commission's transportation jurisdiction is "plenary" and extends to all transactions "except those which Congress has made explicitly subject to regulation by the States." *FPC* v. *Southern California Edison Co.*, 376 U.S. 205, 216 (1964). Further, as this Court has repeatedly stressed, the Commission's power extends to regulating transactions that, if left unregulated, could interfere with the achievement of the goals of the NGA. *Schneidewind* v. *ANR Pipeline Co.*, 485 U.S. 293, 310 (1988); *Transcontinental Gas Pipe Line Corp.* v. *State Oil & Gas Bd. of Mississippi*, 474 U.S. 409, 423-424 (1986); *United Gas Pipe Line Co.* v. *McCombs*, 442 U.S. 529, 538 (1979).

The court of appeals' conclusion that the uniform capacity-release requirements are an appropriate exercise of FERC's jurisdiction over interstate transportation of natural gas (Pet. App. 79a-86a) follows naturally from this Court's rulings that the Commission's transportation jurisdiction extends to, for example, the end-use of the transported gas, see *FPC*

v. *Transcontinental Gas Pipe Line Corp.*, 365 U.S. 1, 7-8, 22 (1961), interruption of interstate transportation service, see *Panhandle Eastern Pipe Line Co.* v. *FPC*, 332 U.S. 507, 523 (1947), curtailment of gas sales, see *LP&L*, 406 U.S. at 641, financing of interstate pipelines, see *Schneidewind*, 485 U.S. at 306, and gas storage, see *id.* at 295 n.1. The court of appeals' decision is consistent with the decisions of all the other circuits that have addressed challenges to FERC's exercise of its transportation jurisdiction.[8]

Moreover, the court of appeals correctly noted that, "[a]s an entirely separate matter," FERC's jurisdiction over abandonments of service supports its regulation of capacity-release transactions because, "[i]n effect, the pipeline is temporarily abandoning service to the releasing shipper and instituting service to the replacement shipper." Pet. App. 80a. Under Section 7(b) and (c) of the NGA, neither abandonment nor ren-

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[8] Other circuits have unanimously held that FERC's jurisdiction extends broadly to all aspects of transportation, including the "initiation, curtailment, quality, quantity, and termination" of gas deliveries. *National Ass'n of Regulatory Util. Comm'rs* v. *FERC*, 823 F.2d 1377, 1385 (10th Cir. 1987). See, *e.g.*, *United Gas Pipe Line Co.* v. *FERC*, 824 F.2d 417, 425 (5th Cir. 1987) (limiting liability for curtailments); *Fort Pierce Util. Auth.* v. *FPC*, 526 F.2d 993, 996-998 (5th Cir. 1976) (curtailment of retail gas sales); *Corning Glass Works* v. *FERC*, 675 F.2d 392, 394-396 (D.C. Cir. 1982) (spreading of costs of liquified natural gas plant built by LDC to service customers within its territory); *Mississippi Pub. Serv. Comm'n* v. *FPC*, 522 F.2d 1345, 1350 (5th Cir. 1975) (compensating end users for losses caused by curtailments), cert. denied, 429 U.S. 870 (1976); *Panhandle E. Pipe Line Co.* v. *FPC*, 232 F.2d 467, 472 (3d Cir.) (control over the functioning of a pipeline's facilities), cert. denied, 352 U.S. 891 (1956).

dition of new service may occur without permission and prior approval of the Commission. 15 U.S.C. 717f(b) and (c).[9]

b. Petitioners incorrectly assert (96-1186 Pet. 18-21; 96-1188 Pet. 14-16) that regulation of LDCs' assignment of transportation capacity rights to gas consumers operating within the LDCs' service areas is tantamount to regulation of local distribution. Capacity-release involves assignment of rights to use firm interstate transportation capacity on high-pressure trunk lines. Those lines are not "local distribution facilities" within the meaning of Section 1(b) of the NGA. See *FPC* v. *East Ohio Gas Co.*, 338 U.S. 464, 470 (1950). FERC has not in Order No. 636 asserted jurisdiction over any activity occurring behind the city gate after the LDC has received gas from an interstate pipeline. Capacity release does not solely affect LDC capacity assignments to end-users located in local service areas, but enables all firm capacity holders, including LDCs, end-users, and marketers, to deliver gas to any existing, out-of-state delivery point on the interstate pipeline upstream of its city gate or usual delivery point. See Pet. App. 271a, 555a. Deliveries of gas to those out-of-state locations under assigned capacity rights cannot be deemed local distribution of gas, nor can any State

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[9] Petitioner NYPSC asserts (96-1188 Pet. 16), without authority, that the court of appeals erred in concluding that the Commission could regulate partial abandonments of service under Section 7 of the NGA. Petitioner's argument that partial abandonments cannot be regulated would create a serious gap in the Commission's regulatory powers and, in any event, ignores the plain requirement of Section 7(b) that a pipeline may not abandon "*any* service," 15 U.S.C. 717f(b) (emphasis added), without Commission approval.

regulate those out-of-state capacity assignments. See *Mississippi River Transmission Corp.* v. *FERC*, 969 F.2d 1215, 1218 (D.C. Cir. 1992); *Michigan Consol. Gas Co.* v. *FERC*, 883 F.2d 117, 121 (D.C. Cir. 1989), cert. denied, 494 U.S. 1079 (1990).

Even where an LDC assigns its firm capacity on an interstate pipeline to a local end-user, settled precedent makes clear that such a transaction does not constitute local distribution of gas. Indeed, the "local distribution" exception to FERC transportation jurisdiction is "confined to [an LDC's] parcelling out function and (probably) even more narrowly, to parcelling out *accompanied by* retail sales." *Public Utils. Comm'n* v. *FERC*, 900 F.2d 269, 276 (D.C. Cir. 1990). Thus, contrary to petitioners' assertions (96-1186 Pet. 16; 96-1188 Pet. 19-20), the court of appeals' application here of Section 1(b)'s established construction is consistent with the holdings of this Court, *e.g.*, *LP&L*, 406 U.S. at 637-638; *East Ohio*, 338 U.S. at 469-470, and other courts of appeals, *Cascade Natural Gas Corp.* v. *FERC*, 955 F.2d 1412, 1418 (10th Cir. 1992); *United Gas Pipe Line Co.* v. *FERC*, 824 F.2d 417, 425 (5th Cir. 1987), and plainly expressed congressional intent, H.R. Rep. No. 709, 75th Cong., 1st Sess. 3 (1937) ("local distribution * * * is made only to consumers *in connection with sales*" (emphasis added; internal quotation marks omitted)).

c. Petitioner AGD incorrectly asserts (96-1186 Pet. 21-24) that FERC has used unbundling to interfere with matters that are traditionally controlled by the States. Petitioner ignores the pivotal fact that States have never regulated the terms and conditions of interstate pipeline transportation. As the District of Columbia Circuit explained in *Public Utils. Comm'n*, 900 F.2d at 276-277:

> In an era when transporters almost invariably bought gas at one end of the pipeline and sold it at the other, gas would normally reach an end user only after a pipeline's retail sale to that user, a transaction unquestionably under the state's control, or after conventional distribution and sale by a local distributor, again clearly subject to state control. * * * Under modern conditions, by contrast, where the end user often owns the gas and uses the pipeline solely for transportation, application of *East Ohio* removes this fulcrum for state power.

See *East Ohio*, 338 U.S. at 469-470; *Cascade Natural*, 955 F.2d at 1421.

Petitioners' contentions (96-1186 Pet. 24-28; 96-1188 Pet. 13-14) that capacity release interferes with state regulation of the LDCs' traditional role as local supplier of natural gas are similarly unfounded. An LDC's use of the capacity-release program is voluntary and is aimed at unused (and presumably unneeded) capacity. See Pet. App. 244a-245a. FERC does not regulate any aspect of the rates for an LDC's retail sale of its system supply or the use of its own facilities; it regulates only the LDC's use of interstate transportation capacity. As the court of appeals observed, Section 1(b) "does not withdraw from FERC's jurisdiction any aspect of the interstate transportation of natural gas." Pet. App. 82a.

Contrary to NYPSC's assertions (96-1188 Pet. 13-14), the uniform capacity-release mechanism is not unfair to end-users who have "paid" for LDC "pipeline capacity" through "state-approved rates." Under Order No. 636, an LDC's customer can guarantee assignment of the LDC's interstate capacity rights by

contracting with the LDC at the FERC-approved, cost-based transportation rate, or at any lower rate that trumps competing offers. Pet. App. 485a. By allowing LDCs to shed unused capacity and thereby lower costs, the capacity-release mechanism benefits consumers.

AGD incorrectly contends (96-1186 Pet. 27-28) that the capacity-release program impairs state efforts to require LDCs to unbundle local transportation service from retail sales. Rather than imposing obstacles, however, FERC's rule facilitates local unbundling by guaranteeing end-users access not only to their own LDCs' released capacity, but also to the capacity released by any other capacity holder who holds rights to a delivery point at or downstream of the LDC's position on the interstate pipeline. See Pet. App. 271a-272a, 495a-497a.[10]

d. AGD also errs in asserting (96-1186 Pet. 14-18) that the Hinshaw Amendment to the NGA, Pub. L. No. 323, 68 Stat. 36, exempts LDCs from the uniform capacity reallocation mechanism. The Hinshaw Amendment exempts from FERC regulation any person engaged in the transportation or sale in inter-

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[10] AGD argues (96-1186 Pet. 27) that Order No. 636 interferes with "blended" capacity programs now being offered by the States. That argument was neither raised before nor addressed by the Commission or the court of appeals, and there is no factual basis in the record to support it. That claim therefore is not properly presented to this Court. See 15 U.S.C. 717r(b) ("No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing."); see also *Sullivan* v. *Louisiana*, 508 U.S. 275, 279 n.1 (1993) (stating that this Court does not ordinarily review issues not raised below).

state commerce of natural gas received "within or at the boundary of a State" and "ultimately consumed within such State." 15 U.S.C. 717(c). Congress enacted the Hinshaw Amendment "to preserve state control over local distributors who purchase gas from interstate pipelines * * * [but] Congress did not intend the amendment to relieve the Commission of jurisdiction over * * * integrated interstate systems." *Louisiana Power & Light Co.* v. *FPC*, 483 F.2d 623, 633 (5th Cir. 1973), cert. denied, 416 U.S. 974 (1974). As the court of appeals explained, "the Commission's authority to regulate capacity release arises from its jurisdiction over the interstate pipeline that consummates the transaction and the subject of the transaction, the interstate transportation of gas, entirely independent of its jurisdiction over the releasing or replacement shippers." Pet. App. 82a n.62. Moreover, in order for the Hinshaw Amendment to apply, the service at issue would have to be subject to effective state regulation. The States cannot effectively regulate the transactions at issue here because they cannot prevent interstate pipelines from discriminating in favor of in-state users at the expense of out-of-state users. The Hinshaw Amendment accordingly has no application to the interstate transactions at issue here.

AGD places great weight on its contention (96-1186 Pet. 17) that the Hinshaw Amendment overruled this Court's decision in *East Ohio*, 338 U.S. at 461. Although *East Ohio*'s holding—that FERC had jurisdiction over an interstate gas pipeline operating in only one State—is no longer the law, the Hinshaw Amendment did not affect the Court's analysis in *East Ohio* of the scope of the Commission's jurisdiction over pipelines that transport gas across state lines. See

Altamont Gas Transmission Co. v. *FERC*, 92 F.3d 1239, 1246 (D.C. Cir. 1996), petition for certiorari pending, No. 96-1179 (filed Feb. 11, 1997); *Public Utils. Comm'n*, 900 F.2d at 275 n.4. Notwithstanding the particular change brought about by the Hinshaw Amendment, this Court and the courts of appeals have continued consistently to rely on *East Ohio* as a correct and otherwise still valid interpretation of the NGA. *E.g.*, *LP&L*, 406 U.S. at 636-637 & n.13; *California* v. *Lo-Vaca Gathering Co.*, 379 U.S. 366, 369 (1965); *Cascade Natural*, 955 F.2d at 1416-1421; *Public Utils. Comm'n*, 900 F.2d at 275.

e. APGA similarly contends (96-1187 Pet. 9-11) that the court of appeals erred in concluding that municipally owned gas companies must comply with the uniform capacity reallocation mechanism when they seek to reassign interstate pipeline capacity. APGA reasons that, because Section 2 of the NGA excludes municipals from the definition of "persons" regulated as "natural gas companies" under the Act, 15 U.S.C. 717a(1)-(3) and (6), FERC may not require that they comply with the terms of FERC's capacity-release program. 96-1187 Pet. 7-8. The court of appeals correctly concluded, however, that "FERC may, consistent with the NGA, require municipalities to comply with its capacity release regulations" because "FERC's transportation jurisdiction extends as a separate matter over capacity release * * * entirely independent of the jurisdictional nature of the releasing and replacement shippers." Pet. App. 84a-85a.

Although FERC lacks jurisdiction to regulate municipals as such, the Commission's jurisdiction over interstate transportation is not limited to natural-gas companies or "persons" engaged in transportation.

Instead, it extends to all interstate transportation of gas, regardless of the parties involved in such transportation. This Court has rejected the contention "that the word 'transportation' in § 1(b) must be construed as applying only to companies engaged in the business of transporting gas in interstate commerce," concluding that "the Act's language did not express any such limitation." *East Ohio*, 338 U.S. at 468. Indeed, the courts have long recognized that municipalities, although not "natural-gas companies" or "persons" under the Act, are nonetheless subject to NGA regulation under those NGA provisions that are not exclusively directed at "natural-gas companies." See, *e.g.*, *California* v. *Southland Royalty Co.*, 436 U.S. 519, 528 (1978); *Public Serv. Co.* v. *FERC*, 587 F.2d 716, 719 (D.C. Cir. 1979). Thus, as the court of appeals observed (Pet. App. 85a), this Court has concluded that the Commission may properly regulate the curtailments of both gas supply and capacity to municipals under its transportation jurisdiction, see *Transcontinental Gas*, 365 U.S. at 20-22; *LP&L*, 406 U.S. at 640—a situation involving allocation of transportation capacity among shippers in compliance with federal mandates that is "strikingly similar" to capacity release. Pet. App. 85a.[11]

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[11] APGA argues (96-1188 Pet. 13-14) that there is a distinction between transactions in the primary and secondary market for pipeline capacity. As we have noted, pages 10-11, *supra*, however, the Commission's jurisdiction over transportation extends to all aspects of interstate pipeline operation. Further, to declare such secondary transactions beyond the Commission's jurisdiction would create an anomalous gap in the comprehensive regulation intended by Congress in enacting the NGA. See *LP&L*, 406 U.S. at 631-632.

APGA further contends (96-1187 Pet. 12-19) that FERC's regulation of municipalities under its transportation jurisdiction conflicts with FERC's own policy established in *Texas Eastern Transmission Corp.*, 51 F.E.R.C. (CCH) ¶ 61,170 (May 11, 1990). The court of appeals correctly rejected that contention. Pet. App. 84a & n.64. In *Texas Eastern*, the Commission authorized firm transportation customers of an interstate pipeline to broker capacity to third parties without the involvement of the carrying pipeline itself. The Commission required such customers to obtain "limited jurisdiction" certificates under Section 7(c) of the NGA because, as brokers, they were within the meaning of NGA Section 1(b). The Commission, however, ruled that municipals were exempt transporting gas from any such certification requirement because they were not "natural gas companies" and therefore not subject to Section 7. See 48 F.E.R.C. (CCH) ¶ 61,248, at 61,873-61,875 (Aug. 22, 1989); 51 F.E.R.C. (CCH) ¶ 61,170, at 61,453-61,454. The capacity brokering arrangements in *Texas Eastern* were performed by capacity holders themselves without pipeline involvement; under Order No. 636, in contrast, FERC regulates capacity assignment by pipelines. The court of appeals thus correctly held that the *Texas Eastern* approach is inapplicable, and that FERC may require municipals' compliance with capacity-release rules as it may require their compliance with other pipeline terms or conditions of interstate transportation service. Pet. App. 84a-85a.[12]

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[12] *Texas Gas Transmission Corp.*, 55 F.E.R.C. (CCH) ¶ 61,208 (May 13, 1991), and *United Gas Pipe Line Co.*, 46 F.E.R.C. (CCH) ¶ 61,060 (Jan. 24, 1989), modified on other grounds, 49 F.E.R.C. (CCH) ¶ 61,166 (Nov. 7, 1989), followed

Finally, there is no merit to APGA's assertion (96-1187 Pet. 19-20) that the Commission's capacity-release mechanism is merely a sham designed to expand its jurisdiction. As the court of appeals observed, under Order No. 636, "[t]he pipelines' role in capacity release is absolutely central, and the transaction itself controls access to interstate transportation capacity." Pet. App. 84a-85a (footnote omitted). Order No. 636 requires pipelines to maintain electronic bulletin boards upon which proposed transactions are posted, administer the rules for operation of the bidding system, and select the successful bidder. In short, as the court observed, capacity release necessarily involves movement of gas in interstate commerce by the assignee of capacity rights because "[b]y controlling such capacity, the assignors are effectively determining by whom, and under what circumstances, gas will be transported and are using the pipeline's facilities as if they were the assignors' facilities." *Id.* at 81a.

2. Petitioner Burlington Resources Oil & Gas Company (Burlington) (No. 96-1189) argues that the court of appeals erred in affirming FERC's conclusion that pipelines allocating long-term transportation rights under the ROFR mechanism do not have to accept bids at less than the maximum, cost-based just and reasonable rate established by the Commission under the NGA. Burlington asserts (96-1189 Pet. 7-9) that the ROFR rule violates the Commission's obligation under the NGA to protect consumers. As the court of appeals concluded, however, "the basic structure of the [ROFR] mechanism provides

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the *Texas Eastern* approach, and APGA's reliance on those decisions (96-1186 Pet. 14) similarly fails to support the petition.

the [customer] protections from pipeline market power required for pre-granted abandonment under [NGA] § 7." Pet. App. 49a; see also *id.* at 54a-55a. The ROFR procedure "guarantees that existing customers may have continued service," and "affords protection to the existing customer against *any* exercise of monopoly power," *id.* at 933a (emphasis added), because the customer will be required to pay, at most, the cost-based just and reasonable rate established by the Commission in a ratemaking proceeding, *id.* at 679a. As the court of appeals observed, the NGA "protect[s] customers against loss of service only if the customer is willing to pay the maximum rate approved in a rate proceeding." *Id.* at 55a. The Commission concluded that the ROFR mechanism "provides more than adequate protection that pipelines will not be able to charge monopoly rates for their service." *Id.* at 672a. This Court approved a very similar pricing mechanism in *Mobil Oil Exploration & Producing Southeast, Inc.* v. *United Distribution Cos.*, 498 U.S. 211 (1991) (upholding FERC rule setting maximum "just and reasonable" rate for gas sold under Natural Gas Policy Act price ceilings, but allowing sellers voluntarily to accept lower prices if market conditions dictate).[13]

Contrary to Burlington's assertions (96-1189 Pet. 11-12), FERC's decision to leave to pipelines' discretion whether to accept below-ceiling bids voluntarily does not encourage anti-competitive behavior. The

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[13] If a pipeline elects to leave capacity idle rather than accept a below-ceiling bid for that capacity, the shipper may also file a petition with the Commission under Section 5 of the NGA claiming that the pipeline's action is "unjust, unreasonable, unduly discriminatory, or preferential." 15 U.S.C. 717d(a).

Commission cannot require a pipeline to accept rates below the cost-based just and reasonable rate ceiling under the Commission's ROFR program. Those rates are, by definition, the lowest rates that ensure pipelines an adequate return on their investment; requiring pipelines to accept a lower rate would put them at risk of under-recovery in violation of the Commission's duty to ensure pipelines sufficient returns and adequate capitalization. See *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) (rates must "assure confidence in the financial integrity" of the regulated entity "so as to maintain its credit and attract capital"); *Permian Basin Area Rate Cases*, 390 U.S. 747, 792 (1968) (rates must "maintain financial integrity, attract necessary capital, and fairly compensate investors for the risks they have assumed, and yet provide appropriate protection for the relevant public interests"); *Associated Gas Distribs.* v. *FERC*, 824 F.2d 981, 1007-1013 (D.C. Cir. 1987), cert. denied, 485 U.S. 1006 (1988).

Burlington also errs in arguing (96-1189 Pet. 12-15) that FERC should have imposed a rate within the zone of approved rates, but below the maximum just and reasonable rate. Burlington relies chiefly on *Associated Gas*. The pricing mechanism approved in *Associated Gas* established a cost-based just and reasonable rate, but allowed pipelines to "consent to selective discounting" down to prescribed minima. 824 F.2d at 1010. That voluntary discounting approach is precisely the approach taken here.[14]

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[14] Burlington misconstrues cases holding that FERC may establish rates within a "zone of reasonableness." See 96-1189 Pet. 14. That test applies to judicial review of the Commission's rates, not to the establishment of those rates in the first

Finally, Burlington errs in asserting (96-1189 Pet. 18-20) that FERC failed to provide a rationale for its decision not to require pipelines to accept discounted rates under the ROFR process, and that the court of appeals supplied its own rationale. The Commission's statement that pipelines "are not required to accept any offer at less than the maximum rate," Pet. App. 673a, correctly reflects existing law on that point. See page 22, *supra*. Each of the rationales relied upon by the court of appeals was also articulated in the Commission's orders. See Pet. App. 671a-673a, 935a-937a. In any event, a reviewing court retains the power to identify the proper construction of the governing law, even if not argued by the Commission. *Arcadia* v. *Ohio Power Co.*, 498 U.S. 73, 77 (1990).

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instance. See *Permian Basin*, 390 U.S. at 767. Burlington also asserts (96-1189 Pet. 16) that the NGA does not guarantee pipelines cost recovery, but only affords them the opportunity to recover their costs. That opportunity, however, must include the possibility of recovering adequate returns on capital investment, which, by definition, turns on the cost-based rate established by the Commission.

CONCLUSION

The petitions for a writ of certiorari should be denied.

Respectfully submitted.

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IN THE
Supreme Court of the United States
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CITIZENS GAS & COKE UTILITY,

Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

REPLY OF PETITIONERS AMERICAN PUBLIC GAS ASSOCIATION AND CITIZENS GAS & COKE UTILITY

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REPLY OF PETITIONERS AMERICAN PUBLIC GAS ASSOCIATION AND CITIZENS GAS & COKE UTILITY

PRELIMINARY STATEMENT

In opposing American Public Gas Association's and Citizens Gas & Coke Utility's (collectively "APGA") petition for a writ of certiorari ("Petition"), FERC merely restates the lower court's holding that FERC has jurisdiction over municipal LDCs' capacity release, "given the involvement of interstate gas pipelines," without offering any analysis or interpretation of Section 2 of the Natural Gas Act ("NGA"), 15 U.S.C. § 717a (1994), which excludes municipal LDCs from FERC's jurisdiction. *See* Br. in Opposition at 17-20. In fact, FERC in large part ignores the "plain language" argument advanced by APGA in its Petition, and thus provides no justifiable basis for denying APGA's Petition.

Since the filing of APGA's Petition, this Court issued a decision recognizing the limitations of FERC's jurisdiction under the express terms of the NGA. *General Motors Corp. v. Tracy*, _____U.S. _____, 117 S. Ct. 811, 136 L. Ed. 2d 761 (1997). This Court stated, as did APGA in its Petition, that the statutory scheme of the NGA was one of cooperative action between federal and local agencies. *Id.* at 821. *See* APGA Pet.

at 10 ("Congress struck the balance between the appropriate realm of federal regulation and the appropriate realm of local regulation and reflected it in the express terms of the NGA."). The *General Motors* decision supports the need for this Court to grant APGA's Petition in order to establish firmly the limits of FERC's authority under the NGA, in accord with Congress' express intent. For the reasons set forth by this Court in *General Motors* and those set forth below, APGA's Petition should be granted.

ARGUMENT

FERC's primary assertion in its opposition is that the Commission's jurisdiction over interstate transportation is not limited to natural-gas companies or "persons" engaged in transportation. Br. in Opposition at 17. That assertion is belied by the express language of the NGA and the legislative framework surrounding it. *See* 15 U.S.C. § 717; *see also* H.R. Rep. No. 709, 75th Cong. 1st Sess. (1937). FERC's suggested interpretation of the NGA, if accepted, would always ratify the exercise of federal authority over municipal LDCs. Such a result contravenes the NGA's exclusion of municipalities under the NGA, and is clearly at odds with Congress' express intent and this Court's recent jurisprudence interpreting the NGA and other Congressional acts. *General Motors,* 117 S. Ct. at 821; *see also Dunn v. Commodity Futures Trading Comm'n,* _____ U.S. _____, 117 S. Ct. 913, 137 L. Ed. 2d 93 (1997).

Moreover, FERC's interpretation of the NGA is not relevant in light of the express language of Section 2. This Court has recently affirmed that an agency's interpretation of a statute which it administers need not be accorded any deference where the language of the statute is clear on its face. *Dunn,* 117 S. Ct. at 920 n.14 (when a statute as a whole "clearly expresses Congress' intention . . . administrative deference is improper."). FERC's obligation is to apply the NGA as Congress wrote it. *Id.* at 916. It failed to do so.

FERC attempts to support its opposition with cases that do not support its main premise and that have no relevance to APGA's exemption claim under NGA Section 2. Instead, the cases upon which FERC relies refer only vaguely, and even then only in some of its cited cases, to the exclusionary provisions of the NGA; no citation supports FERC's position that it can

regulate municipalities under NGA Section 2. The Commission's frail arguments lean on cases involving regulation of high pressure natural gas pipelines, previous dedication of natural gas to interstate commerce and the obligation to serve, and areas in which the Commission alleged that the states were unable to manage effectively.

This is a case involving municipalities' rights to select their own customers, a responsibility they have demonstrated they are capable of performing; it does not entail the dedication of natural gas in interstate commerce, nor does it involve the interpretation of jurisdiction of high pressure gas lines. The critical issue here is whether Congress intended federal authority to govern. *Federal Power Comm'n v. Transcontinental Gas Pipe Line Corp.*, 365 U.S. 1, 27 (1961). Petitioners submit the answer is no, and FERC's attempts to rationalize its conduct by reference to unrelated cases does not change the fact that Congress did not intend FERC to regulate municipalities under Section 2 of the NGA.

Thus, despite FERC's assertions to the contrary, the cited cases where FERC's jurisdiction is upheld *are not* "strikingly similar" to the exercise of jurisdiction over a municipal LDC's capacity release. Br. in Opposition at 18. In fact, in the cases cited by FERC, the Court approved federal regulation *only* after determining that a federal authority was attempting to control a problem that was not, by its very nature, one with which local regulatory authorities could have been expected to deal. *See, e.g., Federal Power Comm'n v. Louisiana Power & Light Co.*, 406 U.S. 621, 641 (1972). As APGA demonstrated in its Petition, that is not the case here. *See generally* APGA Pet. at 9-10.

The *General Motors* case suggests that the cases relied upon by FERC are no longer good law. *See, e.g., General Motors,* 117 S. Ct. at 821. In *General Motors,* the Court recognized the diminished application of cases like *Federal Power Comm'n v. East Ohio Gas Co.,* 330 U.S. 464 (1950)—which had permitted FERC to regulate intrastate activities of LDCs—since Congress subsequently amended the NGA with the Hinshaw Amendment. *See* 15 U.S.C. § 717(c). Nonetheless, FERC leads its opposition to APGA's Petition with the *East Ohio* case. Br. in Opposition at 18.

Surprisingly, in its opposition FERC concedes that its so-called "plenary" transportation jurisdiction does *not* extend to transactions "which Congress has made *explicitly* subject to regulation by the States." Br. in Opposition at 10 (citation omitted) (emphasis supplied). If the Court extends that assertion to its logical conclusion, it must find that any "plenary" jurisdiction that FERC may have under the NGA would *not* extend to entities which Congress *explicitly* exempted.

FERC urges this Court to let the Court of Appeals' decision stand without review—a decision that effectively and unconstitutionally rewrites Congress' express statutory language. This should not be permitted. *Dunn*, 117 S. Ct. at 916.

FERC's exercise of authority over municipal LDCs in contravention of the express exemption in the NGA presents an important constitutional issue for the Court's consideration. Both FERC's actions and the Court of Appeals' ruling negate the express language of a properly enacted federal statute. This Court must ensure both the proper administration of the NGA and the proper review of federal statutes whose language is clear and unambiguous on its face. Here Congress has spoken clearly. The Court of Appeals' decision ignoring the plain meaning of NGA Section 2 is wrong and should be reversed.

CONCLUSION

For the reasons stated herein, the petition for a writ of certiorari should be granted.

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